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No. _____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

TEXAS EASTERN TRANSMISSION CORPORATION,
Petitioner,

v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

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PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the placement of a private corporation's stock in trust for the benefit of a foreign government as part of an insolvency proceeding is sufficient to convert the corporation into a "foreign state" for purposes of federal jurisdiction under the Foreign Sovereign Immunities Act, 28 U.S.C. § 1603(a).

2. Whether, in a case in which federal jurisdiction is premised solely on diversity of citizenship, 28 U.S.C. § 1332(a), a court's assertion of federal jurisdiction over state-law counterclaims against nondiverse parties not originally in the case is consistent with the principles of pendent-party jurisdiction articulated in *Finley* v. *United States*, 490 U.S. 545 (1989).

PARTIES TO THE PROCEEDING

The parties to the proceeding in the court below were petitioner Texas Eastern Transmission Corporation[*/] and the following respondents: Fidelity and Casualty Insurance Company of New York; Associated Electric & Gas Insurance Services, Ltd.; Aetna Casualty and Surety Company; American Home Assurance Company, a/k/a American Home Insurance Company; Boston Old Colony Insurance Company; Cigna Insurance Company; Continental Casualty Company; Employers Mutual Company; First State Insurance Company; Highlands Insurance Company; The Home Insurance Company; The Insurance Company Of North America; Insurance Company Of The State Of Pennsylvania; International Insurance Company; Lexington Insurance Company; Midland Insurance Company; National Surety Corporation; Prudential Reinsurance Company; Ranger Insurance Company; Republic Insurance Company; Stonewall Insurance Company; United States Fire Insurance Company; Certain Underwriters at Lloyd's, London and Certain London Market Insurance Companies.

[*/] In accordance with Supreme Court Rule 29.1, the parent companies and nonwholly owned subsidiaries of petitioner Texas Eastern Transmission Corporation are listed at App. 340-41.

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v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Texas Eastern Transmission Corporation respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinions below of the court of appeals (App. 6-68) are reported at 15 F.3d 1230 (3d Cir. 1994) and 15 F.3d 1249 (3d Cir. 1994). The opinions of the district court (App. 106-312) are unreported.

JURISDICTION

The court of appeals denied a petition for rehearing on February 3, 1994. (App. 4-5.) On April 21, 1994, Justice Souter extended the time for filing a petition for a writ of certiorari to and including July 1, 1994. (App. 1.) The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

28 U.S.C. § 1332(a) provides:

> (a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $50,000, exclusive of interest and costs, and is between —
>
> (1) citizens of different States;
> (2) citizens of a State and citizens or subjects of a foreign state;
> (3) citizens of different States and in which citizens or subjects of a foreign state are additional parties; and
> (4) a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States.
>
> For the purposes of this section, section 1335, and section 1441, an alien admitted to the United States for permanent residence shall be deemed a citizen of the State in which such alien is domiciled.

28 U.S.C § 1603(a) - (b) provides:

For purposes of this chapter —

(a) A "foreign state", except as used in section 1608 of this title, includes a political subdivision of a foreign state or an agency or instrumentality of a foreign state as defined in subsection (b).

(b) An "agency or instrumentality of a foreign state" means any entity —

(1) which is a separate legal person, corporate or otherwise, and
(2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and
(3) which is neither a citizen of a State of the United States as defined in section 1332(c) and (d) of this title, nor created under the laws of any third country.

STATEMENT OF THE CASE

1. Petitioner Texas Eastern Transmission Corporation ("TETCO") owns and operates several natural gas pipelines in a system that extends approximately 10,000 miles from the Gulf Coast of Texas and Louisiana to the New York metropolitan area. TETCO's pipelines use turbine-driven compressors to propel the gas. In 1958, TETCO began using a liquid containing polychlorinated biphenyls ("PCBs") as a lubricant in certain of the compressors. These lubricants eventually mixed with other liquids in the

pipeline system. Over several years, TETCO removed these liquids from the pipeline system and, consistent with standard industry practice, discharged some of these liquids into unlined earthen pits. The liquids in these pits subsequently contaminated the property of TETCO and third parties through overflow and other discharges. In addition, the liquids escaped into the environment from the pipeline system through leaks, spills, and other unintentional discharges.

During the 1980s, TETCO began negotiating with federal and state agencies concerning its statutory responsibilities with respect to the PCB contamination caused by the pipeline liquids. In June 1988, TETCO entered into a consent agreement with the EPA that obligated TETCO to remediate property contaminated by PCBs. TETCO also entered into similar consent decrees with several state environmental agencies. In addition to these cleanup obligations, TETCO incurred liabilities to private third parties for property damage and personal injuries.

2. Respondents are twenty-three insurance companies ("the insurers") that sold approximately 110 policies of primary and excess comprehensive general liability ("CGL") insurance to TETCO between 1958 and 1987. Although the language of the insuring agreement in these policies varies, most of the policies essentially provide that the insurers will indemnify TETCO for "all sums which the insured shall become legally obligated to pay as damages because of bodily injury or property damage caused by an occurrence during the policy period." The policies also require TETCO to provide notice of a claim under the policies "as soon as practicable."

In a letter dated August 19, 1987, TETCO officially

notified the insurers of a claim for coverage under its CGL policies for the sums it was obligated to pay as a result of the PCB contamination from its pipeline system. This insurance claim resulted in the three lawsuits, later consolidated, that are the subject of this petition:

a. *F&C* Case. On December 11, 1987, respondent Fidelity & Casualty Company of New York ("Fidelity" or "F&C"), TETCO's primary CGL carrier throughout the relevant period, sued TETCO in the United States District Court for the Northern District of Texas. Federal jurisdiction was premised on diversity of citizenship. F&C sought a declaratory judgment concerning its duty to defend or indemnify TETCO under the CGL policies for sums paid by TETCO as a result of claims by the EPA, state agencies, and private parties.

b. *AEGIS* Case. On March 11, 1988, respondents Associated Electric & Gas Insurance Services Limited ("AEGIS") and National Surety Corporation ("National Surety") sued TETCO and the remaining insurers in the United States District Court for the Eastern District of Pennsylvania. The *AEGIS* complaint sought a declaratory judgment concerning the plaintiffs' rights and duties under the CGL policies.

Diversity jurisdiction was not available in the *AEGIS* case, because AEGIS shared citizenship with many of the insurer-defendants. Instead, AEGIS and National Surety maintained that federal jurisdiction was proper under the Foreign Sovereign Immunities Act ("FSIA"), 28 U.S.C. §§ 1330(a), 1603(a), 1605(a)(2). FSIA jurisdiction was premised on the contention that one of the insurer-defendants, the Insurance Corporation of Ireland ("ICI"), was a "foreign state" within the meaning of the FSIA.

ICI's alleged foreign sovereign status was based on the following facts, which are not in dispute. ICI was incorporated in the Republic of Ireland as a private company in 1935. As a private corporation, it subscribed to some of the insurance contracts at issue here between 1978 and 1985. By 1985, it became overextended and lacked sufficient reserves to cover its liabilities. Accordingly, pursuant to an order by Ireland's High Court, ICI was placed under "administration," a procedure involving a potentially indefinite period of court protection that is similar to Chapter 11 protection under United States bankruptcy law. As part of this procedure, virtually all of ICI's stock was acquired by Sealuchais Archais Teoranta ("SAT"), a private limited liability company. Since March 18, 1985, the shareholders and directors of SAT have been two individuals who have held their shares in SAT in trust for Ireland's Minister of Industry and Commerce. Neither the Minister nor the Irish government holds legal title to any stock in either ICI or SAT.

c. *Texas Eastern* Case. On March 21, 1988, TETCO filed a comprehensive action in Texas state court against all of its insurers seeking a declaratory judgment and damages under Texas law.[1/] On June 3, 1988, the insurers removed the entire case to the United States District Court for the Southern District of Texas. Removal jurisdiction was asserted under the FSIA solely on the basis of the alleged foreign sovereign status of a single insurer, ICI.

3. On May 31, 1988, the Judicial Panel on

[1/] Texas Eastern had previously filed an essentially identical action against the insurers in New Jersey state court on December 21, 1987. That suit was subsequently dismissed on March 17, 1988, on the ground of *forum non conveniens*.

Multidistrict Litigation transferred the *F&C* case pursuant to 28 U.S.C. § 1407 to the Eastern District of Pennsylvania and consolidated it there with the *AEGIS* case for pretrial proceedings. In July 1988, the United States District Court for the Southern District of Texas transferred the *Texas Eastern* action to the Eastern District of Pennsylvania prior to ruling on TETCO's motion to remand the case to state court. *Texas Eastern* was then consolidated with the other two cases.

Following consolidation of the three cases in the Eastern District of Pennsylvania, TETCO moved to remand the *Texas Eastern* action to Texas state court and to dismiss or stay the *AEGIS* action. In support of these motions, Texas Eastern argued that the court lacked subject-matter jurisdiction because ICI was not a "foreign state" within the meaning of the FSIA. Assuming in the alternative that ICI was a foreign state, TETCO maintained that the service-of-suit clause in the CGL policies constituted a waiver of ICI's right to remove the *Texas Eastern* case.[2/] TETCO also argued that the *AEGIS* case should be dismissed because, after a necessary realignment of the parties based on their true interests, the suit was not "against a foreign state" as is required for jurisdiction under the FSIA, 28 U.S.C.

2/ The service-of-suit clause provides:

> It is agreed that in the event of the failure of the Underwriters hereon [*i.e.*, ICI] to pay any amount claimed to be due hereunder, Underwriters hereon at the request of the Insured (or Reinsured) will submit to the jurisdiction of any Court of competent jurisdiction within the United States and will comply with all requirements necessary to give such Court jurisdiction and all matters arising hereunder shall be determined in accordance with the law and practice of such court.

§ 1330(a). Although TETCO did not challenge subject-matter jurisdiction in the *F&C* case (because at that time the *F&C* case involved only the diverse parties TETCO and F&C), it did move to stay or dismiss the *F&C* case in deference to the more comprehensive *Texas Eastern* case.

At a hearing on September 15, 1988, the district court rejected TETCO's jurisdictional arguments. (App. 282-312.) The court held that, once the shares of ICI's holding company, SAT, were placed in trust for the benefit of the Irish Minster of Industry and Commerce, ICI automatically became a "foreign state" under the FSIA. (App. 295-98.) In addition, the court held that the parties in the *AEGIS* case were properly aligned for purposes of federal jurisdiction under the FSIA (App. 293-95), and that ICI had not waived its right to remove the *Texas Eastern* case to federal court, (App. 302-04). Finally, the court rejected TETCO's motion to stay or dismiss the *F&C* case. (App. 306.)

After the district court rejected TETCO's jurisdictional arguments, TETCO filed an answer in the *F&C* case and asserted counterclaims against the single plaintiff, F&C. In addition, as a precautionary measure, TETCO joined its twenty-two excess insurers (six of which shared the same citizenship as TETCO) "as co-defendants in the counterclaims" (App. 13), pursuant to Fed. R. Civ P. 13(h).

Following limited discovery, the parties filed cross-motions for summary judgment. The district court granted the insurers' motion, holding that TETCO was barred from recovering against the insurers because it had failed to provide them with timely notice of the matters for which it would seek coverage. (App. 106-281.)

TETCO appealed the district court's rulings on both the

jurisdictional issues and the merits. On May 28, 1993, the court of appeals affirmed the district court in an unpublished opinion. (App. 76-103.) The court held that ICI "qualifies as a 'foreign state' because the Republic of Ireland owns 100% of its stock and has assumed its obligations." (App. 81.) The court further rejected TETCO's arguments that ICI had waived its right to remove the *Texas Eastern* case and that ICI should be realigned as a party plaintiff in the *AEGIS* case. (App. 81-82 & n.1.) Finally, the court affirmed the district court's conclusions concerning late notice. (App. 83-92.) Judge Alito filed a dissenting opinion. (App. 93-103.)

On June 10, 1993, TETCO filed a petition for panel rehearing and suggestion for rehearing in banc, arguing that the panel opinion's jurisdictional rulings conflicted with precedents from the Third Circuit and other Circuits. Over the next several months, both TETCO and the insurers filed additional documents with the court of appeals concerning, *inter alia*, whether the excess insurers were properly joined in the *F&C* case pursuant to TETCO's counterclaims against F&C, and, if so, whether the court possessed ancillary or pendent jurisdiction over the nondiverse excess insurers. On August 18, 1993, the original panel issued an order granting TETCO's request for rehearing and asking the parties to address three questions: "1) [T]he structure and purpose of 28 U.S.C. § 1330; 2) [W]hat claims, if any, have been asserted by AEGIS against ICI; [and] 3) [W]hether the presence of all parties destroys supplemental jurisdiction in the *F&C* case." (App. 74.)

After supplemental briefing and reargument, the original panel issued an opinion for publication reaching the same jurisdictional conclusions that it had reached in its

earlier decision. (App. 6-48.)[3/] The court once again rejected TETCO's argument that ICI was not a "foreign state" within the meaning of the FSIA:

> We uphold the district court's finding that ICI is a "foreign state" within the meaning of 28 U.S.C. § 1603(a). The district court has determined that ICI is an "agency or instrumentality of a foreign state" in that it is a separate legal person, a majority of its shares are owned by a foreign state, the Republic of Ireland, and it is neither a citizen of a state of the United States, nor created under the laws of a third country. These findings are not clearly erroneous.

(App. 23 n.8.) The court also again rejected TETCO's waiver and realignment arguments, albeit for reasons somewhat different than those expressed in its earlier decision. (App. 21-36.)

In addition, the court of appeals rejected TETCO's arguments regarding the scope of jurisdiction in the *F&C* case. The court first held that the excess insurers were properly joined to the counterclaims TETCO asserted against F&C. (App. 16-17.) The court then rejected TETCO's contention that the district court's exercise of subject-matter jurisdiction over the counterclaims against the nondiverse excess insurers was a form of pendent-party jurisdiction precluded by the Supreme Court in *Finley* v. *United States*, 490 U.S. 545 (1989). Relying on this Court's decision in *Owen Equipment & Erection Co.* v.

[3/] The Third Circuit issued two opinions, one discussing jurisdiction (App. 6-49) and the other discussing the merits (App. 50-69).

Kroger, 437 U.S. 365, 376 (1978), and a pre-*Finley* Third Circuit decision, the court distinguished (and thus refused to apply) *Finley* on the "subtle" ground that claims against the nondiverse parties in the *F&C* case were asserted by a defendant rather than a plaintiff. (App. 17-19.) The court concluded that the "additional non-diverse counterclaim defendants do not destroy diversity jurisdiction in the *F&C* action because there is complete diversity of citizenship between the original named parties." (App. 21.)

Judge Alito again dissented. "Assuming that ICI falls within 28 U.S.C. § 1603's definition of a 'foreign state,'" Judge Alito argued that the majority erred in concluding that it had jurisdiction in the *Texas Eastern* and *AEGIS* cases under the FSIA. (App. 38-45.) Judge Alito declined to consider TETCO's arguments concerning joinder and jurisdiction in the *F&C* case. Instead, he would have vacated the *Texas Eastern* and *AEGIS* cases and remanded the *F&C* case to the district court for an initial determination of whether the excess insurers were properly joined and "whether, despite *Finley*, the district court could exercise subject matter jurisdiction over the counterclaims." (App. 45-48.)

Following this decision, TETCO filed a petition for rehearing, which was denied on February 3, 1994. (App. 4-5.)[4/]

[4/] The district court recently held a status conference concerning matters collateral to the three cases and granted a stay of all such matters pending resolution of this certiorari petition. (App. 2-3.)

REASONS FOR GRANTING THE PETITION

This petition presents two important issues of federal jurisdiction, both of which implicate conflicts of authority in the lower courts.

I. THERE IS A CONFLICT IN THE COURTS REGARDING WHETHER THE PLACEMENT OF A PRIVATE CORPORATION'S STOCK IN TRUST FOR THE BENEFIT OF A FOREIGN GOVERNMENT AS PART OF AN INSOLVENCY PROCEEDING IS SUFFICIENT TO CONVERT THE CORPORATION INTO A "FOREIGN STATE" FOR PURPOSES OF FEDERAL JURISDICTION UNDER THE FOREIGN SOVEREIGN IMMUNITIES ACT.

The FSIA defines a "foreign state" to include "a political subdivision of a foreign state or an agency or instrumentality of a foreign state." 28 U.S.C. § 1603(a). "Agency or instrumentality" is in turn defined in relevant part as "any entity . . . which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof." 28 U.S.C. § 1603(b)(2).

In both the district court and the court of appeals, TETCO argued that ICI is not a "foreign state" under the FSIA because (a) the Irish government has at most an indirect ownership interest in ICI's shares, (b) the government does not exercise control over ICI's operations, and (c) ICI does not serve a public purpose. The lower courts, however, concluded that the "administration" procedure described above, whereby the stock of ICI's holding company, SAT, was placed in trust for the benefit

of the Irish Minister for Industry and Commerce, was sufficient to convert ICI into a foreign state.

The lower courts' determination that ICI is a "foreign state" under the FSIA directly conflicts with decisions by district courts in three other Circuits, which have held that ICI is *not* a "foreign state" under the FSIA. *See Aluminum Co. of America* v. *Admiral Ins. Co.*, No. C93-32C (W.D. Wash. Apr. 9, 1993) (App. 313-15); *Murphy Oil USA, Inc.* v. *United States Fidelity & Guar. Co.*, No. 91-1157, 1992 WL 465701 (W.D. Ark. Dec. 21, 1992) (App. 316-31); *Mobil Corp.* v. *Abeille Gen. Ins. Co.*, No. H-89-3877, 1990 WL 504828 (S.D. Tex. Nov. 6, 1990) (App. 332-39), *appeal dismissed*, 984 F.2d 664 (5th Cir. 1993). Another court has specifically noted the "conflicting opinions" on this issue. *Tennessee Gas Pipeline Co.* v. *Continental Casualty Co.*, 814 F. Supp. 1302, 1306 n.6 (M.D. La. 1993).

This division is the functional equivalent of a conflict in the Circuits, because the three district court decisions holding that ICI is not a foreign state (and therefore remanding the cases back to state court) were not appealable. Except in certain civil rights cases, "[a]n order remanding a case to the State court from which it was removed is not reviewable on appeal or otherwise." 28 U.S.C. § 1447(d). Section 1447(d) has specifically been applied to bar appellate review in a case holding that ICI is not a foreign state. *See Mobil Corp.* v. *Abeille General Ins. Co.*, 984 F.2d 664, 666 (5th Cir. 1993).

There could not be a clearer conflict of authority: different courts have reached opposite conclusions regarding the "foreign state" status of the *very same entity*, ICI. They did so despite their application of the same statute, 28 U.S.C. § 1603, to the same facts concerning the Irish

government's relationship with ICI.

In *Mobil*, the court emphasized that "[n]either the Minister for Industry and Commerce nor the Irish government holds legal title to any stock in either ICI or SAT." (App. 334.) The court went on to hold that, "[e]ven if the Irish government has an ownership interest in ICI *this courts jurisdiction is not automatic*." (*Id.* (emphasis added).) Rather, the court looked to two "'more precise indices'" of an entity's status: "'the degree to which the entity discharges a governmental function, and the extent of state control over the entities operations.'" *(Id.)* (quoting *Edlow International Co.* v. *Nuklearna Elektrarna KRSKO*, 441 F. Supp. 827, 832 (D.D.C. 1977)). Those "more precise indices" are precisely the factors that the lower courts in this case refused to consider.[5/]

This issue of the "foreign state" status of foreign companies that become insolvent and have their shares placed in trust is of widespread significance, especially in the insurance industry. With increasing environmental and other liabilities, many foreign insurers are now facing potential insolvency. This is particularly true in the London insurance market, of which ICI is a part, where over a dozen insurers have become insolvent in the last several

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[5/] In *Murphy Oil*, the court reviewed the *Mobil* decision at length and found its reasoning and conclusions "persuasive." (App. 330.) In *ALCOA*, the court reviewed both *Mobil* and *Murphy Oil*, found them "persuasive," and, indeed, believed that the issue was sufficiently clear that ICI should be barred from further claiming that it is a "foreign state." (App. 315.)

years.[6] The use of trust and similar arrangements, whereby the shares of private corporations are held for the benefit of foreign governments, is thus likely to increase substantially in the future.

The lower courts' rulings — which allow private companies to become "foreign states" simply by virtue of trust arrangements established as part of insolvency proceedings — could therefore lead to massive abuse of the procedural and substantive rights granted under the FSIA. It will mean that, as in this case, essentially private insurance companies like ICI will be able to:

- defeat otherwise-valid contractual choice-of-forum clauses;[7]
- use artificial pleading arrangements to create federal jurisdiction;[8]

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[6] Richard Lapper, *Crisis Reaches Small Insurance Companies; Problems in Lloyd's Market Have Spread,* Financial Times, Jan. 14, 1993, at 21.

[7] At the time that ICI agreed to the service-of-suit clause in the insurance policies at issue in this case, it was indisputably a private corporation. Courts (including the Third Circuit) normally interpret such clauses to constitute a waiver of the right to remove a case to federal court. *See, e.g., Foster* v. *Chesapeake Ins. Co.*, 933 F.2d 1207 (3d Cir.), *cert. denied,* 112 S.Ct. 302 (1991). Nevertheless, the court below held that ICI's post-contractual transformation into a "foreign state" rendered ICI's waiver unenforceable. (App. 35-36. *But see* App. 42 (Alito, J., dissenting).)

[8] Faced with a lack of diversity jurisdiction, the plaintiff-insurers in the *AEGIS* case named ICI — another insurer with identical interests — as a party defendant in a declaratory judgment suit so that the case would appear to be "against a foreign state" for purposes of obtaining FSIA jurisdiction.

- manipulate removal, transfer, and consolidation provisions so that a federal court unfamiliar with the state law at issue decides the case;[9] and

- bring other similarly-interested companies with no claim to "foreign state" status along with them into federal court.[10]

In another case involving the Insurance Corporation of Ireland, this Court reiterated the fundamental principle that federal courts are courts of limited jurisdiction and that the boundaries of their subject-matter jurisdiction must be strictly maintained. *Insurance Corp. of Ireland* v. *Compagnie des Bauxites de Guinee*, 456 U.S. 694, 701-02 (1982). This Court should grant review to resolve the conflict in the courts regarding ICI's status and to enforce the proper limits of federal subject-matter jurisdiction.

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[9] The district court acknowledged at oral argument on summary judgment that it "ha[d]n't the faintest what Texas law is" (Hearing Tr. Jan. 13, 1992, at 31), and its opinion noted "the difficulty and irony of a federal district court judge sitting in Pennsylvania predicting what the Supreme Court of Texas would do if faced with particular questions, given that two of the three cases consolidated in this action originated in Texas and concern activities which primarily occurred there." (App. 122 n.12.) Judge Alito's dissent reiterated the oddity of the federal courts in the Third Circuit deciding "difficult, unsettled, and controversial questions of Texas insurance law" based on "erroneous jurisdictional premises." (App. 38 (Alito, J., dissenting).)

[10] The twenty-three respondent-insurers were present in federal court in the *Texas Eastern* and *AEGIS* lawsuits only because ICI had subscribed, as a foreign private corporation, to a few of the many policies of excess coverage obtained by TETCO through one of TETCO's many insurers, Lloyd's of London. ICI was liable for at most $8 million of the billions of dollars of insurance coverage potentially at issue.

II. THE ASSERTION BY THE COURT OF APPEALS OF FEDERAL JURISDICTION OVER TETCO'S CLAIMS AGAINST THE NONDIVERSE EXCESS INSURERS IS INCONSISTENT WITH THIS COURT'S DECISION IN *FINLEY* v. *UNITED STATES*, AND CONFLICTS WITH A DECISION IN THE FIFTH CIRCUIT.

TETCO argued before the court of appeals that the assertion of federal jurisdiction in the *F&C* case over the counterclaims filed against the nondiverse excess insurers under Rule 13(h) was prohibited by this Court's decision in *Finley* v. *United States*, 490 U.S. 545 (1989). The court of appeals' rejection of this argument is inconsistent with *Finley* and directly conflicts with the Fifth Circuit's decision in *Birmingham Fire Ins Co. of Pa.* v. *Winegardner and Hammons, Inc.*, 714 F.2d 548 (5th Cir. 1983).

In *Finley*, this Court considered whether a party suing the federal government under the Federal Tort Claims Act ("FTCA"), 28 U.S.C. § 1346(b), could also assert against a private party a claim for which there was no independent basis of federal jurisdiction. The Court stated that this issue involved the validity of "pendent party jurisdiction," which the Court defined broadly as "jurisdiction over parties not named in any claim that is independently cognizable by the federal court." 490 U.S. at 549 (emphasis omitted). Relying on three prior Supreme Court decisions,[11/] the Court held that "a grant of jurisdiction over claims involving particular parties does not itself confer jurisdiction over additional claims by or against different parties." *Id.*

11/ *Owen Equip. & Erection Co.* v. *Kroger*, 437 U.S. 365 (1978); *Aldinger* v. *Howard*, 427 U.S. 1 (1976); *Zahn* v. *International Paper Co.*, 414 U.S. 291 (1973).

at 556. Because the FTCA did not expressly authorize federal jurisdiction over the additional claim brought against the additional party, the Court dismissed the claim. *Id.*

The claims against the nondiverse excess insurers in this case, like the claims against the pendent party in *Finley*, are "added claims involv[ing] added parties over whom no independent basis of jurisdiction exists." *Id.* at 551. *Finley*'s prohibition of federal jurisdiction over claims against such pendent parties applies when the primary claim is brought under the diversity statute, for as the *Finley* Court made clear, that statute authorizes jurisdiction over suits between "citizens of different States *and no one else*." *Id.* at 552 (emphasis added). Accordingly, *Finley* prohibits the assertion of federal jurisdiction over the claims against the nondiverse excess insurers.

Relying on a misinterpretation of dicta in this Court's decision in *Owen Equipment & Erection Co.* v. *Kroger*, 437 U.S. 365 (1978), and on a pre-*Finley* Third Circuit decision, the court of appeals attempted to distinguish *Finley* on the "subtle" ground that the pendent-party claims here were brought by a defendant "haled into court against his will" rather than by a plaintiff who initiated the lawsuit. *Finley*, however, addressed and rejected essentially the same argument. After noting that, "unlike in *Kroger*, the party seeking to bring the added claims had little choice but to be in federal rather than state court, since the FTCA permits the Federal Government to be sued only there," the *Finley* Court held that "*that [difference] alone is not enough*" to permit pendent-party jurisdiction. *Finley, 490 U.S.* at 552 (citation omitted) (emphasis added). In addition, in response to Justice Stevens' dissent, the *Finley* Court made clear that its elimination of pendent-party jurisdiction extended to third-party claims under Fed. R. Civ. P. 14(a), which include claims made by defendants haled into court

against their will. *Id.* at 553 n.6.

The decision below thus flies in the face of *Finley*. It also directly conflicts with the Fifth Circuit's decision in *Birmingham Fire Ins Co.* v. *Winegardner and Hammons, Inc.*, 714 F.2d 548 (5th Cir. 1983). There, a Texas corporation owned a hotel that was damaged by a hurricane. One of its insurers, a Pennsylvania corporation, initiated a diversity action seeking a declaratory judgment under state law with respect to its liability. The defendant hotel asserted a state-law counterclaim against that insurance company and a second, nondiverse Texas insurer. Relying on *Aldinger* and *Kroger*, the Fifth Circuit held that it lacked jurisdiction over the counterclaim against the nondiverse insurer. *Id.* at 552-54.

Birmingham Fire is in direct conflict with the decision below. In both cases, a plaintiff-insurer brought a state-law coverage suit under the diversity statute, and the defendant-insured asserted counterclaims against the original plaintiff and additional nondiverse insurers not previously in the case. Although both courts relied primarily on this Court's decision in *Kroger*, they reached antithetical conclusions: *Birmingham Fire* rejected the assertion of jurisdiction over the pendent parties, while the court below permitted it. In addition, the Fifth Circuit expressly rejected the Third Circuit's rationale based on *Kroger* for asserting federal jurisdiction:

> [*Kroger*] is analytically indistinguishable from the case now before us. Although there it was the plaintiff which initiated all the litigation, whereas in this case Holiday Inn is a cross-plaintiff and did not originate the litigation but rather was forced to answer BFI's motion for declaratory judgment, that distinction is not

> significant. And it is certainly not enough to overcome the general diversity requirement.

Id. at 553.

The conflict with *Finley* and *Birmingham Fire* implicates important issues of federal-state relations. *Finley*'s strict rule of construction for federal jurisdiction statutes derives from the constitutional concern of protecting state prerogatives. 490 U.S. at 552-53; *see also id.* at 577 (Stevens, J., dissenting) (noting lack of federal interest in resolution of state law claim of pendent party when jurisdiction based on diversity of citizenship). As this Court has long made clear:

> The power reserved to the states under the Constitution to provide for the determination of controversies in their courts, may be restricted only by the action of Congress in conformity to the Judiciary Articles of the Constitution. Due regard for the rightful independence of state governments, which should actuate federal courts, requires that they scrupulously confine their own jurisdiction to the precise limits which the statute has defined.

Shamrock Oil & Gas Corp. v. *Sheets*, 313 U.S. 100, 108-09 (1941) (citations omitted). This federalism principle has special force in a case involving insurance law, which both Congress and this Court have recognized is the special province of the states. *See* McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015; *United States Dep't of the Treasury* v. *Fabe*, 113 S. Ct. 2202, 2207 (1993) (purpose of McCarran-Ferguson Act is "broadly to give support to existing and future state systems for regulating and taxing the business of insurance").

In sum, the exercise of jurisdiction over the counterclaims against the nondiverse excess insurers is inconsistent with *Finley* and *Birmingham Fire*, and impermissibly intrudes on state-law prerogatives.[12/]

[12/] Although the Court below correctly noted that the new supplemental jurisdiction statute, 28 U.S.C. § 1367 (Supp. 1992), does not apply in this case (App. 20), it nonetheless maintained that its assertion of jurisdiction over the counterclaims against the nondiverse excess insurers was consistent with the new statute (App. 20-21). This dictum is based on an erroneous reading of Section 1367 that further demonstrates the continuing significance of this case. Section 1367(b) reaffirmed *Finley*'s prohibition on pendent-party jurisdiction in diversity cases -- the point at issue here. Section 1367(b) provides that "the district courts shall *not* have supplemental jurisdiction . . . over claims by plaintiffs against persons made parties under Rule 14, 19, 20, or 24 of the Federal Rules of Civil Procedure." (Emphasis added.) TETCO asserted the counterclaims against the nondiverse excess insurers under Rule 13(h); the nondiverse excess insurers were therefore necessarily joined as counterclaim defendants pursuant to Rule 19 or 20. *See, e.g.*, Fed. R. Civ. P. 13(h) (authorizing counterclaims against "[p]ersons other than those made parties to the original action . . . *in accordance with the provisions of Rules 19 and 20*") (emphasis added). Thus, contrary to the dictum of the court below, Section 1367(b) would (if it applied) prohibit a court from exercising supplemental jurisdiction in a case like this one. *See, e.g., Mayatextil, S.A.* v. *Liztex U.S.A., Inc.*, No. 92 Civ. 4528, 1993 U.S. Dist. LEXIS 6527, at *7 (S.D.N.Y. May 18, 1993) ("Congress intended § 1367(b) to encompass Rule 13(h)."); *see also* Denis F. McLaughlin, *The Federal Supplemental Jurisdiction Statute — A Constitutional and Statutory Analysis*, 24 Ariz. St. L.J. 849, 940 n.471 (1992); Karen Nelson Moore, *The Supplemental Jurisdiction Statute: An Important But Controversial Supplement to Federal Jurisdiction*, 41 Emory L.J. 31, 56 n.82 (1992).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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June 1994

Supreme Court, U.S.
FILED

93207 0 JUN 2 4 1994

No. _____

OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1993

TEXAS EASTERN TRANSMISSION CORPORATION,
Petitioner,

v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

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APPENDIX

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SUPREME COURT OF THE UNITED STATES

No. A-790

Texas Eastern Transmission Corporation

Petitioner

v.

Fidelity and Casualty Insurance Company of

New York, et al.

ORDER

UPON CONSIDERATION of the application of counsel for the petitioner,

IT IS ORDERED that the time for filing a petition for a writ of *certiorari* in the above-entitled case, be and the same is hereby, extended to and including July 1st, 1994.

Associate Justice of the Supreme
Court of the United States

Dated this 21st day of April, 1994

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

FIDELITY AND CASUALTY COMPANY OF NEW YORK	:	
v.	:	CIVIL ACTION NO. 92-4804
TEXAS EASTERN TRANSMISSION CORPORATION, et al.	:	
TEXAS EASTERN TRANSMISSION CORPORATION	:	
v.	:	CIVIL ACTION 93-15
FIDELITY AND CASUALTY COMPANY OF NEW YORK, et al.	:	

ORDER

After a conference held on the record on April 21, 1994, it is ORDERED as follows:

1. The parties, either jointly or separately shall submit, as soon as practical, by letter, a status report as to any and all outstanding motions pending in Civil Actions 92-4804 and 93-15, together with a statement as to the date of filing of said motions, and the date of filing any answer, response, reply, or other pleading to said motions, if any, by any and all parties.

2. Upon representations by Texas Eastern Transmission Corporation that it will seek a writ of

certiorari from The Supreme Court of the United States to review the final decisions of the United States Court of Appeals for the Third Circuit *In re Texas Eastern Transmission Corporation PCB Contamination Insurance Coverage Litigation, MDL 764*, Civil Actions 92-4804 and 93-15 shall be stayed pending final decision by The Supreme Court of the United States, or until further order of this court. This order staying proceedings is without prejudice to any party to seek to remove the stay if such party, in good faith, thinks it will be seriously prejudiced by further delay or that the petition for *certiorari* is not being promptly filed or processed.

3. While the present stay of Civil Actions 92-4804 and 93-15 is in effect, no party in these actions shall file in any court any additional action seeking a determination of insurance coverage by or for Texas Eastern Transmission Corporation for PCB contamination, irrespective of whether further claims are filed or asserted by third parties against Texas Eastern Transmission Corporation for PCB contamination damage; provided, however, that during the period of this stay the statute of limitations for filing any action to determine such insurance coverage issue shall be tolled.

BY THE COURT:

_____

Donald W. VanArtsdalen, S.J.

April 21, 1994

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 92-1638

IN RE TEXAS EASTERN
TRANSMISSION CORPORATION
PCB CONTAMINATION INSURANCE
COVERAGE LITIGATION

SUR PETITION FOR REHEARING

Present: BECKER, STAPLETON, MANSMANN, GREENBERG, HUTCHINSON, SCIRICA, COWEN, NYGAARD, ALITO, ROTH, LEWIS and ALDISERT,*
Circuit Judges.

The petition for rehearing filed by appellant in the above entitled case having been submitted to the judges who participated in the decision of this court and to all other available circuit judges of the circuit in regular active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of

the circuit in regular active service not having noted for rehearing by the court *in banc,* the petition for rehearing is denied. Judge Greenberg would have granted rehearing.

BY THE COURT,

_____

Circuit Judge

*Senior Circuit Judge Aldisert voted only as to panel rehearing.

A-6

Filed January 10, 1994

OPINION 1 OF 2

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 92-1638

IN RE: TEXAS EASTERN TRANSMISSION CORP. PCB CONTAMINATION INSURANCE COVERAGE LITIGATION
(MDL No. 764)

ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD.; NATIONAL SURETY CORPORATION

v.

TEXAS EASTERN TRANSMISSION CORPORATION; FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK; CERTAIN UNDERWRITERS AT LLOYDS OF LONDON, INCLUDING THE INSURANCE COMPANY OF IRELAND; AETNA CASUALTY AND SURETY COMPANY; AMERICAN HOME ASSURANCE COMPANY; BOSTON OLD COLONY INSURANCE COMPANY; CONTINENTAL CASUALTY INSURANCE COMPANY; FIRST STATE INSURANCE COMPANY; HIGHLANDS INSURANCE COMPANY; THE HOME INSURANCE COMPANY; INSURANCE COMPANY OF NORTH AMERICA; INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA; INTERNATIONAL INSURANCE COMPANY; LEXINGTON INSURANCE COMPANY; MIDLAND INSURANCE COMPANY; MUTUAL MARINE INSURANCE COMPANY; PRUDENTIAL REINSURANCE COMPANY; RANGER INSURANCE COMPANY; REPUBLIC INSURANCE COMPANY; STONEWALL INSURANCE COMPANY; PENNSYLVANIA INSURANCE GUARANTY ASSOCIATION; UNITED STATES OF AMERICA; UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
(D.C. Civil No. 88-02126)

A-7

THE FIDELITY & CASUALTY CO. OF NEW YORK

v.

THE TEXAS EASTERN TRANSMISSION CORP.
(D.C. Civil No. 88-05039)

TEXAS EASTERN TRANSMISSION CORPORATION

v.

FIDELITY AND CASUALTY COMPANY OF NEW YORK; ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD.; AETNA CASUALTY AND SURETY COMPANY; AMERICAN HOME ASSURANCE COMPANY, a/k/a AMERICAN HOME INSURANCE COMPANY; BOSTON OLD COLONY INSURANCE COMPANY; CIGNA INSURANCE COMPANY; CONTINENTAL CASUALTY COMPANY; EMPLOYERS MUTUAL CASUALTY COMPANY; FIRST STATE INSURANCE COMPANY; HIGHLANDS INSURANCE COMPANY; THE HOME INSURANCE COMPANY; THE INSURANCE COMPANY OF NORTH AMERICA; INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA; INTERNATIONAL INSURANCE COMPANY; LEXINGTON INSURANCE COMPANY; MIDLAND INSURANCE COMPANY; NATIONAL SURETY CORPORATION; PRUDENTIAL REINSURANCE COMPANY; RANGER INSURANCE COMPANY; REPUBLIC INSURANCE COMPANY; STONEWALL INSURANCE COMPANY; UNITED STATES FIRE INSURANCE COMPANY; CERTAIN UNDERWRITERS AT LLOYD'S, LONDON and CERTAIN LONDON MARKET INSURANCE COMPANIES
(D.C. Civil No. 88-05707)

Texas Eastern Transmission Corporation,

Appellant

Appeal from the United States District Court
for the Eastern District of Pennsylvania

A-8

Argued
April 7, 1993

Before: MANSMANN, ALITO and ALDISERT,
Circuit Judges.

Reargued
September 30, 1993

(Filed January 10, 1994)

OPINION OF THE COURT

MANSMANN, Circuit Judge.

This is a companion opinion to *Fidelity & Casualty Co. of New York v. The Texas Eastern Transmission Corp.*, 15 F.3d 1249 (3d Cir. 1994), an opinion filed today which affirms the district court's determination of liability in three cases consolidated for appeal before us. The three cases are *Fidelity & Casualty Co. of New York v. The Texas Eastern Transmission Corp.*, (hereinafter the "*F & C*" action) originally filed in the Northern District of Texas, *Texas Eastern Transmission Corp. v. Fidelity and Casualty Co. of New York et al.*, (hereinafter the "*Texas Eastern*" action) originally filed in a Texas state court and later removed to the Southern District of Texas, and *Associated Electric & Gas Insurance Services Ltd. et al. v. Texas Eastern Transmission Corp. et al.* (hereinafter the "*AEGIS*" action) filed in the Eastern District of Pennsylvania. All three cases were later assigned by the Multi-District Litigation Panel to the district court below.

This opinion discusses the question of subject matter jurisdiction in the *Texas Eastern* action and the AEGIS action. We also address the question of jurisdiction in the *F & C* case to the extent that its jurisdiction based on diversity is impacted by our discussion of subject matter jurisdiction in the other two cases. That our discussion has to be bifurcated in two separate opinions results from a procedural anomaly: Texas Eastern sought rehearing in only two of the three cases — *Texas Eastern* and *AEGIS* — and only on the question of subject matter jurisdiction.

At issue in this panel rehearing is the district court's exercise of subject matter jurisdiction in *Texas Eastern* and *AEGIS* arising from insurance coverage for the cost of toxic PCB clean-up. The claims were filed after Texas Eastern Transmission Corporation's release, discharge and disposal into the environment of PCB-contaminated substances in the course of operating a natural gas pipeline extending from Texas and Louisiana to New Jersey.

Texas Eastern, the insured, appealed the decision of the district court, which granted summary judgment to Texas Eastern's insurance carriers, primarily on the basis that Texas Eastern breached its duty to provide the carriers timely notice of matters for which it would seek coverage, and in this way prejudiced the carriers. *In Re Texas Eastern Transmission Corp. PCB Contamination Insurance Coverage Litigation*, No. MDL-764 (E.D. Pa. July 9, 1992). We affirmed in an unreported opinion filed May 28, 1993, after confirming that the district court had subject matter jurisdiction over all three cases. In the first of the three actions, the *"F & C"* action, subject matter jurisdiction was based on diversity of citizenship, 28 U.S.C. § 1332, and was not and is not now being contested by Texas Eastern. Subject matter jurisdiction in the remaining two actions, the *"AEGIS"* action and the *"Texas Eastern"* action, was derived from the Foreign Sovereign Immunities Act, 28 U.S.C. § 1330 (original) and § 1441(d) (removal).

Thereafter, Texas Eastern filed a petition for rehearing challenging subject matter jurisdiction in the two cases. On August 18, 1993, we ordered panel rehearing and stayed the mandate in all three cases consolidated in this appeal. On January 6, 1994, we vacated our unreported opinion.

This opinion addresses the jurisdictional issues raised in the petition for rehearing, which was directed *only* to the

question of subject matter jurisdiction in *AEGIS* and *Texas Eastern*. In addition, because Texas Eastern contended on appeal and reasserted on rehearing that the district court lacked jurisdiction over the counterclaim defendants in the *F & C* case, and hence should have stayed *F & C* in favor of an allegedly more comprehensive action which Texas Eastern had commenced in a Texas state court, we address this challenge to the district court's jurisdiction in *F & C*. In a separate opinion filed simultaneously with this, we in effect reinstate the portion of our earlier opinion addressing the substantive merits of the issues on appeal from the order of the district court, as these issues were not challenged in the petition and were not the subject of the rehearing. *See Dunn v. Hovic*, 1 F.3d 1362, 1993 U.S. App. LEXIS 20182 (July 27, 1993) (reinstating earlier opinion as to matters not subject of rehearing *in banc*); *Dunn v. Hovic*, 1 F.3d 1371, 1993 U.S. App. LEXIS 19482 (July 27, 1993) (addressing only those issues which were subject of rehearing *in banc*).

I.

A brief statement of the facts appears in the related opinion filed simultaneously with this one. A more detailed statement of the facts appears in the district court's opinion. Here we outline the nature of the three cases in question and the jurisdictional challenges raised in the petition for rehearing.

After Texas Eastern's August 1987, notice to its insurers that it was negotiating with federal and state agencies over the PCB contamination of several of its properties, Fidelity & Casualty Company of New York, Texas Eastern's primary excess liability insurer, filed the first of the three actions, the "*F & C* action," in the United States District Court for the Northern District of Texas, seeking a declaratory judgment disclaiming liability.

Subject matter jurisdiction was premised on diversity and is not challenged. Texas Eastern unsuccessfully moved to dismiss or stay the *F & C* action in favor of a New Jersey state court action which Texas Eastern had already commenced against all of its insurers.[1/]

In the second action, the *"AEGIS"* action, two of Texas Eastern's excess insurers, Associated Electric and Gas Services, Ltd. and National Surety Corporation, filed a comprehensive declaratory judgment action against Texas Eastern and its other insurance carriers, primary or excess, in the United States District Court for the Eastern District of Pennsylvania. The district court premised original subject matter jurisdiction over the *AEGIS* case on the Foreign Sovereign Immunities Act (FSIA), 28 U.S.C. § 1330, based on the presence as a party defendant of the Insurance Company of Ireland, Ltd., (ICI). ICI is a "foreign state" under 28 U.S.C. § 1603(a) of the FSIA having no immunity with regard to the commercial claims brought against it in the *AEGIS* action. The Immunities Act provides for federal jurisdiction in civil commercial actions brought "against" a foreign state.

The third and final action, the *"Texas Eastern"* action, was commenced by Texas Eastern in a Texas state court against all of its insurers, seeking declaratory judgment and damages. This action was, in effect, a refiling of the earlier dismissed action which Texas Eastern had initiated in the New Jersey state court. Pursuant to 28 U.S.C. § 1441(d) of the FSIA, ICI removed *Texas Eastern* to the United

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[1/] The action in the New Jersey state court was titled *Texas Eastern Transmission Corporation v. Fidelity & Casualty Company*, and was docketed as No. WO-30685-87 (N.J. Sup. Ct., filed December 19, 1987). It was dismissed on March 17, 1988, on the ground of *forum non conveniens*. Texas Eastern did not appeal the dismissal.

States District Court for the Southern District of Texas. Section 1441(d) permits removal of a civil action "against a foreign state" as the term "foreign state" is defined in 28 U.S.C. § 1603.

The *F & C* action was transferred to the federal district court in eastern Pennsylvania and consolidated with *AEGIS* for pretrial proceedings. The *Texas Eastern* action was also consolidated for pretrial purposes with *AEGIS* after it was removed to the federal court.

In seeking *vacatur* of the district court's judgment in all three cases and to adjudicate its coverage claims in state court, *Texas Eastern* argues that the district court erroneously assumed FSIA jurisdiction; hence, it argues that the *Texas Eastern* case should have been remanded to the Texas state court, the *AEGIS* case should have been dismissed for lack of subject matter jurisdiction, and the *F & C* case should have been sent back to the Texas federal court where it likely would have been dismissed or stayed in deference to the state court proceeding.

Texas Eastern does not challenge diversity jurisdiction between the original parties in the *F & C* case, yet in our view we deem it significant that in the *F & C* case, Texas Eastern committed itself to two important actions: (1) it asserted counterclaims against F & C and (2) it joined all other parties in these combined cases as co-defendants in the counterclaims. What started out as an action between only The Fidelity & Casualty Co. of New York and Texas Eastern then became, through Texas Eastern's actions, a case involving *all* the carriers in this litigation.

On appeal from the district court's grant of summary judgment in favor of the insurers, however, Texas Eastern asserts a contention that it did not raise below: now, for

the first time, it argues that jurisdiction over the counterclaim was improper. Texas Eastern further asserts that, assuming ICI is a foreign state within the meaning of § 1603, FSIA jurisdiction over *AEGIS* was precluded by mandatory realignment of the parties, which would have adjusted ICI's nominal status as defendant to plaintiff. Furthermore, Texas Eastern asserts that ICI contractually waived any right it had under the FSIA to remove in the *Texas Eastern* case.

We have jurisdiction over a final decision of the district court pursuant to 28 U.S.C. § 1291. We rehear matters which were the subject of our opinion of May 28, 1993, pursuant to Federal Rules of Appellate Procedure 35 and 40.

II.

We address the question of jurisdiction in each of the three cases *seriatim*. The substantive merits of the district court's holding in favor of the insurance carriers is addressed in an opinion filed simultaneously with this one. *Fidelity & Casualty Co. of New York v. The Texas Eastern Transmission Corp.*, 15 F.3d 1249 (3d Cir. 1994).

A. The *F & C* Case

On December 11, 1987, the *F & C* declaratory judgment action against Texas Eastern was commenced in federal district court in Texas. Texas Eastern filed an answer with counterclaims against virtually all of its excess insurers on December 15, 1988, after the *F & C* case had been transferred to the Eastern District of Pennsylvania and consolidated with the remaining two related cases. Although diversity jurisdiction between the two original parties, F & C and Texas Eastern, is undisputed, Texas

Eastern now claims that the district court lacked jurisdiction over its counterclaims because Texas Eastern failed to state a basis in the Federal Rules of Civil Procedure for adding the excess insurers, failed to seek leave of court to join them, and did not execute service of process upon them; hence they were not made parties to the suit and the *F & C* action involved only the policies issued by its primary liability carrier.[2] *Fidelity and Casualty Co. of N.Y. v. Texas Eastern Transmission Corp.*, No. 88-5039.

Texas Eastern mounts the following argument. The complaint by F & C tracked a very narrow compass because it involved only primary carrier liability. Outstanding at the same time in two other lawsuits was the question of liability of both primary and excess carriers. Therefore, had not the district court erroneously assumed it had jurisdiction over Texas Eastern's excess liability carriers in *F & C*, the district court would have dismissed the *F & C* law suit in favor of the more comprehensive state court action.[3]

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[2] The district court's decision at p. 7 granted summary judgment "on *all* claims against [the carriers]," and the order and judgment of the district court was entered in favor of "*all the carriers* and against Texas Eastern." Docket No. 88-5039, second entry of July 10, 1992 (emphasis added). Texas Eastern's failure to appeal that entry of judgment in the *F & C* action may be construed as a waiver of its present contention that the excess carriers were not proper parties in the *F & C* action. Because we find ample other reason to reject Texas Eastern's jurisdictional challenge to the *F & C* case, the issue of Texas Eastern's waiver need not dispose of this matter.

[3] The panel is in unanimous agreement that at this very late juncture in the prosecution of the *F & C* action it would be extremely imprudent to remand this cause on the basis of what amounts to conjecture on the part of Texas Eastern, which cannot call into question the competence of a federal court to resolve matters of substantive state law. Although

(continued...)

1.

In deciding whether the excess insurers were parties to the *F & C* action, we note preliminarily that a party is deemed to have consented to personal jurisdiction if the party actually litigates the underlying merits or demonstrates a willingness to engage in extensive litigation in the forum. *In Re Real Estate Title and Settlement Services Antitrust Litigation*, 869 F.2d 760, 771 (3d Cir.), *cert. denied*, 493 U.S. 821, 110 S. Ct. 77, 107 L. Ed. 2d 44 (1989). The *F & C* counterclaim defendants actively litigated the *F & C* action, failed to move to dismiss Texas Eastern's counterclaim for lack of service before litigating the motions for summary judgment, and, in fact, moved for summary judgment on other grounds.[4/] Thus, we may

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[3/](...continued)
Judge Alito disagrees with the majority opinion on other grounds, he joins the majority in this regard.

[4/] In a supplemental stipulation regarding cross-claims and counterclaims entered into by F & C and the excess insurers, and approved and ordered by the district court on January 17, 1989, F & C and the excess insurers preserved the excess insurers' cross-claims in the *F & C* action. With the exception of the initial pleadings, the excess insurers failed to object to lack of service or *in personam* jurisdiction in the *F & C* case. In its answer and counterclaim, Texas Eastern asserted that "*[A]ll* of Texas Eastern's insurers must bear, *jointly and severally*, all indemnity, damages, defense costs, costs, and reasonable attorney's fees resulting from any of the foregoing claims," belying Texas Eastern's own belief that its excess insurers were party to the *F & C* action, and undermining Texas Eastern's attempt to separate its claims against F & C from its claims against the excess insurers. Furthermore, Texas Eastern's motion for leave to amend pleadings included the excess insurers in the caption. Not only did the excess insurers respond on the merits, but the district court ruled, in an order of July 25, 1991, to dismiss all or specific claims against certain of the excess insurers,

(continued...)

infer that the counterclaim defendants effectively waived the defense of lack of personal jurisdiction based on the absence of service of process by acquiescing in personal jurisdiction. *See Zelson v. Thomforde*, 412 F.2d 56, 58-59 (3d Cir. 1969); *United States v. Article of Drug*, 362 F.2d 923, 926-27 (3d Cir. 1966). Since service of process is to provide notice of the pendency of the action, which the excess carriers clearly had, and goes to the question of *in personam* jurisdiction, in which the excess carriers have clearly acquiesced, the district court's exercise of personal jurisdiction over the excess carriers in the *F & C* action cannot be nullified by Texas Eastern's failure to cause summonses to be served on them. The district court implicitly adopted such a holding when it entered judgment in the *F & C* action "in favor of all carriers," and we affirm this resolution of the question of personal jurisdiction in *F & C*.

2.

Having disposed of contentions regarding personal jurisdiction, we must now consider the claim that the district court lacked subject matter jurisdiction over the non-diverse counterclaim defendants in the *F & C* action. In its counterclaim, Texas Eastern alleged ancillary jurisdiction over the excess insurers. Ancillary subject matter jurisdiction may be exercised over additional party defendants to a compulsory counterclaim, or over third

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[4](...continued)
evidencing its assumption that the excess insurers were indeed parties to the *F & C* action. Finally, the district court's order and final judgment of July 9, 1992, granted "final judgment on *all claims* in favor of *all insurance carriers*." (Emphasis added.) This order was individually entered on the docket in all three cases, including the *F & C* action. Docket No. 88-5039, second entry of July 10, 1992.

party defendants. *See Great Lakes Rubber Corp. v. Herbert Cooper Co.*, 286 F.2d 631, 633-34 (3d Cir. 1961) (ancillary jurisdiction extends to subject matter of counterclaim arising out of transaction or occurrence which is subject matter of opposing party's claim of which court has jurisdiction, and such counterclaim is "compulsory"); *Field v. Volkswagenwerk AG*, 626 F.2d 293, 299 (3d Cir. 1980) (no independent jurisdictional basis required for third party claim when diversity jurisdiction obtained over original claim). Nevertheless, Texas Eastern now claims that the district court's exercise of subject matter jurisdiction over the counterclaims against the non-diverse excess insurers was a form of pendent party jurisdiction precluded by the Supreme Court in *Finley v. United States*, 490 U.S. 545, 109 S. Ct. 2003, 104 L. Ed. 2d 593 (1989) (declining to exercise pendent party jurisdiction under Federal Tort Claims Act unless statute conferring jurisdiction over primary claim explicitly confers jurisdiction over pendent party claim). Texas Eastern argues that neither the diversity statute, 28 U.S.C. § 1332, upon which jurisdiction over the original claim lies, nor any other arguably applicable federal statute, authorizes such jurisdiction over the excess insurers.[5/]

[5/] Texas Eastern further claims that the district court could have assumed personal jurisdiction over the excess insurers only by virtue of the discretionary authority represented in Federal Rule of Civil Procedure 13(h). Rule 13(h) provides that: "[p]ersons other than those made parties to the original action may be made parties to a counterclaim or cross-claim in accordance with the provisions of Rules 19 and 20." Because, *inter alia*, the court made no explicit reference to its discretionary power to join the counterclaim defendants, Texas Eastern argues that the court did not properly exercise its discretionary authority.

(continued...)

In this regard, we note initially that the Supreme Court has carefully distinguished a non-federal claim asserted by a *plaintiff* which can be joined with a federal cause of action arising from the same transaction despite its destruction of complete diversity, from ancillary jurisdiction, which typically involves "claims by a defending party haled into court against his will, or by another person whose rights might be irretrievably lost unless he could assert them in an ongoing action in federal court." *Owen Equipment and Erection Co. v. Kroger*, 437 U.S. 365, 376, 98 S. Ct. 2396, 57 L. Ed. 2d 274 (1978). *See also Ambromovage v. United Mine Workers of America*, 726 F.2d 972, 989 n.48 (3d Cir. 1984) ("ancillary" jurisdiction pertains to claims other than those of plaintiff, such as compulsory counterclaims, while "pendent" jurisdiction pertains to plaintiff's non-federal claims where there is a federal claim which gives the court jurisdiction). This subtle distinction places in doubt Texas Eastern's broad reading of *Finley*.

5/(...continued)

Moreover, Texas Eastern asserts that Rule 13(h) prohibits Texas Eastern's counterclaim inasmuch as under the Rule a "'counter-claim . . . may not be directed solely against persons who are not already parties to the original action . . .'". Texas Eastern's letter brief, September 8, 1993, at p. 19 (citing *Baltimore & Ohio R. Co. v. Central Ry. Services, Inc.*, 636 F. Supp. 782, 786 (E.D. Pa. 1986)).

We find Texas Eastern's argument to be without merit because, as we indicate in our opinion, we hold that the district court implicitly found *in personam* jurisdiction over the excess insurers. Furthermore, Texas Eastern's counterclaim was not directed solely against the counterclaim defendants, but requested the court adjudge that "*all* of Texas Eastern's insurers must bear, *jointly and severally*, all indemnity, damages, defense costs . . . ". Answer and counterclaim of defendant Texas Eastern, December 15, 1988, at p. 40 (emphasis added).

We note secondly that Congress has confirmed the principle of ancillary jurisdiction over counterclaim defendants in the enactment of the Judicial Improvements Act of 1990, 28 U.S.C. § 1367 (using new statutory term, "supplemental jurisdiction").[6/] Section 1367(b) of the Act restricts the extension of jurisdiction in diversity cases over "claims by *plaintiffs* against persons made parties under Rule 14, 19, 20, or 24," (emphasis added), and by its terms would not extend to Texas Eastern's counterclaims as party defendant. "Supplemental" jurisdiction under the statute extends to any related claim of the defendant that arises out of the same case or controversy as the original claim. *See* C. Wright, A. Miller, M. Kane, *Federal Practice and Procedure Civil 2d,* § 1436 at 11 (Supp. 1993); *see, also,* C. Wright, *Federal Courts* § 79 at 527 n.6 (4th ed. 1983) ("the bringing in of additional parties to respond to a

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[6/] For the present purposes, § 1367(a) and (b) are of interest and read as follows:

> (a) . . .[I]n any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. Such supplemental jurisdiction shall include claims that involve the joinder or intervention of additional parties.
>
> (b) In any civil action of which the district courts have original jurisdiction founded solely on section 1332 of this title, the district courts shall not have supplemental jurisdiction under subsection (a) over claims by plaintiffs against persons made parties under Rule 14, 19, 20 or 24 of the Federal Rules of Civil Procedure, or over claims by persons proposed to be joined as plaintiffs under Rule 19 of such rules, or seeking to intervene as plaintiffs under Rule 24 of such rules, when exercising supplemental jurisdiction over such claims would be inconsistent with the jurisdictional requirements of section 1332.

compulsory counterclaim does not destroy diversity jurisdiction"). Thus, it would appear that the Judicial Improvements Act would preserve jurisdiction in the *F & C* action.[7/] We hold that the additional non-diverse counterclaim defendants do not destroy diversity jurisdiction in the *F & C* action because there is complete diversity of citizenship between the originally named parties.

3.

Having found that federal jurisdiction was correctly found in the *F & C* case and that all of the insurers are parties to that action, we note the possibility that the principle of ancillary jurisdiction might again be invoked to ground subject matter jurisdiction in the remaining two cases, *AEGIS* and *Texas Eastern*. We need not rely here on the principle of ancillary jurisdiction, however, because we find an independent source of federal subject matter jurisdiction in both cases.

B. The *AEGIS* Case

The second of the actions that was before the district court, *Associated Electric & Gas Insurance Services, Ltd. v. Texas Eastern Transmission Corp.*, No. 88-2126, was filed by two of Texas Eastern's excess carriers on March 11, 1988 in the United States District Court for the Eastern District of Pennsylvania, in which were joined as defendants

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7/ The Judicial Improvement Act of 1990 became operative on December 1, 1990, well after the *F & C* action was filed. We make reference to the Act merely to evidence the viability of the principles which have generated the doctrine of ancillary jurisdiction in light of the doubt cast upon such jurisdiction by *Finley*. We are satisfied however that the Judicial Improvement Act codifies the implications of the Court's distinctions in *Owen Equipment*.

with Texas Eastern all other insurers, including ICI. Based on the presence of the foreign state, ICI, as a party "against" which a nonjury civil trial was brought, jurisdiction in federal court was pursuant to 28 U.S.C. §§ 1330(a) and 1603.[8/] Texas Eastern argued that the

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[8/] The Foreign Sovereign Immunities Act, Pub. L. No. 94-583, 90 Stat. 2892 (Oct. 21, 1976) (FSIA), establishes the jurisdiction of the federal courts in cases involving foreign sovereigns and the rights of foreign sovereigns with regard to their non-immune commercial or private acts to have actions brought against them adjudicated in a federal bench trial. 28 U.S.C. § 1603 of the FSIA and its jurisdictional provision, 28 U.S.C. § 1330, provide respectively that,

28 U.S.C. § 1603:

(a) A "Foreign state," . . . includes a political subdivision of a foreign state or an agency or instrumentality of a foreign state . . .

(b) An "agency or instrumentality of a foreign state" means any entity —

(1) which is a separate legal person, corporate or otherwise, and

(2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and

(3) which is neither a citizen of a State of the United States . . . nor created under the laws of any third country.

28 U.S.C. § 1330:

> The district courts shall have original jurisdiction without regard to amount in controversy of any nonjury civil action against a foreign state as defined in section 1603(a) of this title as to any claim for relief *in personam* with respect to which the foreign state is not entitled to immunity either

(continued...)

defendant insurers in the *AEGIS* action, most notably ICI, should be realigned with AEGIS as plaintiffs to reflect their alleged substantive party designations, making the suit no longer "against" a foreign state, and thus depriving the district court of FSIA subject matter jurisdiction. The district court concluded that the principle of realignment is inapplicable in matters in which subject matter jurisdiction is predicated on something other than diversity of citizenship. The district court found that the *AEGIS* case was "against a foreign state" within the meaning of the FSIA and exercised its jurisdiction over the matter.

In support of its argument for realignment, Texas Eastern argues that the primary purpose of the *AEGIS* action was to obtain a declaratory judgment that Texas Eastern was not entitled to coverage under any of the policies issued to it by the two excess carrier plaintiffs, and that ICI had a common interest with the excess carriers on that primary issue against Texas Eastern. Texas Eastern reasons analogously that, under principles of realignment developed in the context of the federal diversity jurisdiction statute, the court was obliged to realign the nominal parties to reflect their actual adversity of interest on the primary dispute as a prerequisite to deciding whether a basis for jurisdiction

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[2](...continued)

under sections 1605-1607 of this title or under any applicable international agreement.

We uphold the district court's finding that ICI is a "foreign state" within the meaning of 28 U.S.C. § 1603(a). The district court has determined that ICI is "an agency or instrumentality of a foreign state" in that it is a separate legal person, a majority of its shares are owned by a foreign state, the Republic of Ireland, and it is neither a citizen of a state of the United States, nor created under the laws of a third country. These findings are not clearly erroneous.

remained under the FSIA. Texas Eastern argues that because ICI as well as the remaining insurers nominally designated as defendants should have been realigned with the two excess carriers who brought suit, the action was not "against a foreign state," and the jurisdictional authority of the FSIA was improperly invoked to obtain jurisdiction.[2/] We disagree.

1.

It is beyond cavil that federal law determines whether the elements of federal jurisdiction, original or removal, have been satisfied. Here, of course, we must decide whether the *AEGIS* action is "against" ICI, as required under § 1330. Given this explicit jurisdictional requisite, it is self-evident that Congress conditioned its conferral of jurisdiction on the substantive party alignment of any purported *FSIA* action. Thus we are obliged to ascertain the real adversity of interest between AEGIS and ICI in the *AEGIS* case and to realign them according to their substantive interests before recognizing § 1330 jurisdiction.

It is also widely recognized that in enacting the FSIA and related statutory amendments, Congress sought to create a new division in addition to federal question and diversity jurisdiction for federal subject matter jurisdiction. *See, e.g., Ruggiero v. Compania Peruana de Vapores*, 639 F.2d 872 (2d Cir. 1981). It is further evident that enactment of the FSIA was in response to unique policy considerations touching on the international relations of the United States,

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[2/] Because a number of the excess carriers share common citizenship with Texas Eastern, diversity jurisdiction was precluded. Thus, if the principle of realignment had been applied as Texas Eastern advocated, there would not remain any basis for federal jurisdiction over the *AEGIS* action.

considerations not apropos to the federal diversity statute. Indeed, the Supreme Court has acknowledged Congress' deliberate intent to circumvent much of the potential for interference with the federal government's foreign relations caused by lack of uniformity and local bias in civil caselaw involving foreign states as defendants by channelling private actions against foreign sovereigns away from the state forums and into federal courts to be adjudicated in nonjury trials. *Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480, 497, 103 S. Ct. 1962, 76 L. Ed. 2d 81 (1983); *see also* H. R. Rep. No. 94-1487, 94th Cong., 2d Sess. 13 (1976), *reprinted in* 1973 U.S.C.C.A.N. 6611-12. Thus, the FSIA establishes the federal district courts as the forum preferred by Congress for bringing suit against a foreign state, and the policy of "jealous restriction" which has characterized application of the diversity statute is not operative in the FSIA context. *City of Indianapolis v. Chase National Bank*, 314 U.S. 63, 76, 62 S. Ct. 15, 86 L. Ed. 47 (1941) (Congress created diversity jurisdiction with "jealous restriction"). It is with this in mind that we apply the principle of realignment to the *AEGIS* case.

2.

The landmark Supreme Court precedent applying the principle of realignment states,

> Diversity jurisdiction cannot be conferred upon the federal courts by the parties' own determination of who are plaintiffs and who defendants. It is our duty, as it is that of the lower federal courts, to "look beyond the pleadings and arrange the parties according to their sides in the dispute." *Dawson v. Columbia Trust Co.*, 197 U.S. 178, 180, [25 S. Ct. 420, 421,

> 49 L. Ed. 713 (1905)] . . . . Whether the necessary "collision of interests," *Dawson v. Columbia Trust Co.*, *supra*, at 181 [25 S. Ct. at 421], exists, is therefore not to be determined by mechanical rules. It must be ascertained from the "principal purpose of the suit," *East Tennessee, V. & G. R. v. Grayson*, 119 U.S. 240, 244, [7 S. Ct. 190, 30 L. Ed. 382 (1886)], and the "primary and controlling matter in dispute," *Merchants' Cotton Press Co. v. Insurance Co.*, 151 U.S. 368, 385 [14 S. Ct. 367, 373, 38 L. Ed. 195 (1894)].

City of Indianapolis v. Chase National Bank, 314 U.S. 63, 69-70, 62 S. Ct. 15, 86 L. Ed. 47 (1941).

This landmark explication presents a two-tiered methodology for judicial implementation of the federal diversity statute. The first step obliges the federal court to isolate the "primary purpose" or "primary and controlling matter" in a multiple claim suit. The court then directs its attention exclusively to this "primary" or substantively most significant claim in order to facilitate ascertainment of whether the statutory requisites of diversity jurisdiction have been met. This "primary purpose" test, which ranks issues according to their substantive importance in the lawsuit, reflects the approach appropriate to a restrictive and limited jurisdictional mandate, as in the case of the diversity statute. It appears, in fact, to be uniquely well suited to the express language and broad policy objectives of § 1332. We have indeed adopted this test when determining that jurisdiction is properly based on diversity of citizenship. *See, e.g., Employers Insurance of Wausau v. Crown Cork and Seal Co., Inc.*, 905 F.2d 42, 46 (3d Cir. 1990) (requiring a "real dispute on a primary issue in the controversy" for purposes

of the diversity jurisdiction statute). The "primary purpose" test, however, appears much less well suited to the purposes of § 1330, which embodies an effort on the part of Congress to *encourage* rather than merely *permit* litigation in the federal courts.

The second step involved in implementing the jurisdictional mandate at issue in the Court's landmark diversity realignment case obliges the federal courts to "look beyond the pleadings and arrange the parties according to their sides in the dispute." This step, though sometimes conflated with the first step in a diversity analysis and hence commonly identified with diversity jurisprudence, in fact represents a broader principle of judicial interpretation of statutes conferring jurisdiction in federal courts, where the statutory conferral of jurisdiction is predicated upon the adversarial relationship of the parties.[10/] In other words, where party designations have

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[10/] Although the "realignment" of parties typically occurs as part of a federal court's determination of diversity of citizenship, the Supreme Court has "realigned" nominal parties in at least one case where diversity of citizenship indisputably created grounds for original jurisdiction in the federal district court, and was not challenged. *Chicago, R.I. & P.R. Co. v. Stude*, 346 U.S. 574 (1954). In *Stude*, state law provided for appeal to a state court from an administrative condemnation proceeding instituted under state law and resulting in a damages award to a landowner. The petitioner filed an appeal in state court, designating the landowner as "plaintiff" and the petitioner as "defendant," as was required also by state law. The petitioner subsequently sought to remove the state court proceeding on the ground that 28 U.S.C. § 1441, the relevant federal removal statute, authorized "the defendant or the defendants" to remove civil actions brought in a state court of which the federal court has original jurisdiction. In the context of examining the merits of a motion to remand, the Court decided that the procedural provisions of the state law were not controlling for purposes of construing the federal removal statute. *Id.*,

(continued...)

jurisdictional consequences under the relevant federal jurisdiction statute, be it § 1332 diversity, § 1330 FSIA or their related removal provisions, the principle of "realignment" obliges the court to penetrate the nominal party alignment and to consider the parties' actual adversity of interest for purposes of determining whether there is a statutory basis for jurisdiction. Thus, despite some confusion in nomenclature caused perhaps by the commonplace application of "realignment" in the diversity context, the principle embodied by the term "realignment" is one of broader application and is not reducible to the "primary purpose" test utilized in the diversity context. It is incumbent upon us in the present appeal to consider whether a complex FSIA case warrants departure from the "primary issue" analysis which we have adopted in the context of diversity jurisdiction, and application of a more inclusive realignment analysis.

With this in mind, we note that other circuits have rejected the "primary purpose" test in favor of the more lenient "substantial controversy" test to determine § 1330 jurisdiction where multiple claims are pleaded. *See, e.g., American Motorists Insurance Company v. Trane Company*, 657 F.2d 146, 149 (7th Cir. 1981) (substantial controversy

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[10](...continued)
346 U.S. at 580. Thus the fact that the case was docketed in state court with the petitioner as "defendant" was not dispositive for purposes of the right to remove. The Court "realigned" the parties in conformity with their substantive adversity of interest, and held that remand was proper. The Court realigned the parties not to effectuate the limits of diversity jurisdiction, which would not have been vitiated by realignment, but rather to enforce the separate limits on removal jurisdiction. Thus, it is clear that the obligation of the federal courts to realign parties to reflect their true adversity of interest for purposes of deciding the statutory basis for jurisdiction is not limited to cases purportedly based on § 1332.

applied to diversity action). Under the "substantial controversy" ranking of issues standard, the court determines, as precursor to potential realignment, which of the conflicts asserted in the litigation are merely "substantial," and then whether the parties in question are really opposed according to their true interests in any of their substantial conflicts. Under this standard, it would not defeat jurisdiction if there were no statutory basis for jurisdiction on the primary issue in the litigation, as long as the statutory elements of jurisdiction were present on any other "substantial" issue.

In an even more lenient approach than the "substantial controversy" test, a federal court might recognize a plaintiff/defendant relationship of adversity if real adversity exists between the parties on *any* issue asserted in the plaintiff's complaint, regardless of the relative significance of that issue. Such a liberal approach has not been applied to diversity cases in any circuit, as well it ought not given the restrictive language and policy of § 1332. The present complex FSIA case, however, being one of first impression in our circuit, leads us to examine whether it is warranted here. We are guided in this determination by consideration of the structure and purpose of the FSIA and related statutes.

3.

In letter and spirit, a liberal approach in implementing the FSIA's comprehensive jurisdictional scheme is most conducive to the FSIA's paramount objectives of keeping federal courts open to foreign states, and indeed of affirmatively encouraging private actions against foreign states to be adjudicated in federal court. *See Verlinden B.V. v. Central Bank of Nigeria*, 461 U.S. 480, 488-89, 103 S. Ct. 1962, 1968-69, 76 L. Ed. 2d 81 (1983); H.R. Rep. No.

94-1487, 94th Cong., 2d Sess. 6 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6611. Unlike the diversity statute, § 1330 grants original jurisdiction in the district court without regard to the amount in controversy in order to facilitate this policy. Similarly, § 1441(d) confers an absolute right of removal on the defendant foreign state. Thus, the judicial trend to constrict federal diversity jurisdiction does not inform our application of the principle of realignment here. We hold that the restrictive "primary issue" test does not comport with the statutory language or legislative intent of the FSIA. Because the "substantial controversy" test is more than adequately satisfied in the *AEGIS* action, we need not decide whether only minimal adversity need exist between the party bringing the action and the foreign state in order to trigger § 1330 original jurisdiction and § 1441(d) removal jurisdiction.

Applying the substantial controversy standard, we note preliminarily that Texas Eastern itself raises substantial claims against ICI in all three actions, contravening its assertion that ICI is an insignificant party. Moreover, in the *AEGIS* action, AEGIS has sought the adjudication of its rights and obligations *inter se* with respect to the other insurers, including ICI. AEGIS sought a declaration of entitlement to relief by way of contribution or indemnification from ICI and the other insurers; hence, ICI was subject to potential liability, which the district court found to be more than seven million dollars.[11/] ICI was

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[11/] In the *AEGIS* complaint AEGIS alleged a dispute between "plaintiffs and some or all of the Defendant Insurers [as to] whether and to what extent each is obligated to provide insurance coverage to Texas Eastern with respect to the Underlying Environmental Matters." *AEGIS* complaint, ¶ 35. In the Ad Damnum Clause, AEGIS demanded a declaration of "the respective rights and obligations of plaintiffs, each

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indeed haled into court by AEGIS against its will and must be afforded the special protection of the FSIA. Texas Eastern cross-claimed and counterclaimed in the *AEGIS* action asserting joint and several liability among the insurers, including ICI, and not limited to the excess insurers as between themselves.[12/] Thus, while on the primary issue in *AEGIS* there is not a collision of interests between AEGIS and ICI, there is certainly an element of adversity between AEGIS and ICI sufficient to satisfy § 1330's requisite that an action brought "against" a foreign sovereign. Although the district court erroneously reasoned that realignment was a principle associated exclusively with

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11/(...continued)
Defendant Insurer, the United States, EPA, and Texas Eastern, *inter se*, with respect to insurance coverage for the amounts expended or to be expended by Texas Eastern regarding the Underlying Environmental Matters."

12/ In response to a question from our panel regarding the adversity of interest between the syndicates or groups of syndicates of individual entities and limited partnerships organized under the laws of Great Britain for the purpose of selling insurance, collectively referred to as Lloyds, and ICI, which participated in one or more syndicates of Lloyds, counsel for the insurers responded

> There is an issue as to whether [the discharge of PCB from 89 sites along the pipeline over a protracted period of time] constitutes one occurrence or multiple occurrences. AEGIS is a first-layer excess insurer in the middle to late '70s. Other excess insurers sit above it. If there is a finding that there are multiple occurrences, the loss is spread numerous times over the primary and low-layer excess insurance companies and would never come up vertically to the higher layer excess insurers. However, if there is a finding of a single occurrence, Texas Eastern has made a claim of $ 750 million against its insurers [and liability would run vertically].

Transcript of argument on panel rehearing at p. 39-40.

diversity jurisdiction, we will affirm the conclusion of the district court that § 1330 subject matter jurisdiction over the *AEGIS* case was proper.

C. The *Texas Eastern* Case

Texas Eastern Transmission Corp. v. Fidelity & Casualty, No. 88-5707,[13] the third action before the district court, was filed on March 21, 1988, in Harris County, Texas, against all insurers and removed to the United States District Court for the Southern District of Texas by ICI, pursuant to 28 U.S.C. § 1441(d).[14] It was then transferred to the Eastern District of Pennsylvania by order of the Southern District Court dated July 7, 1988. Texas Eastern contends that a service of suit clause appearing in policies subscribed by ICI in favor of Texas Eastern constitutes a waiver of ICI's right of removal under

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[13] In filing this case Texas Eastern was in substance refiling its earlier action against all of its insurers brought in New Jersey state court, *Texas Eastern Transmission Corporation v. Fidelity & Casualty Company*, docketed as No. WO-30685-87, and dismissed on March 17, 1988. This earlier state court action formed the basis for Texas Eastern's motion to dismiss or stay the *F & C* action which was then pending in the Northern District of Texas.

[14] Section 1441(d) provides:

> (d) Any civil action brought in a State court against a foreign state as defined in section 1603(a) of this title may be removed by the foreign state to the district court of the United States for the district and division embracing the place where such action is pending. Upon removal the action shall be tried by the court without jury. Where removal is based upon this subsection, the time limitations of section 1446(b) of this chapter may be enlarged at any time for cause shown.

28 U.S.C. § 1441(d).[15] Texas Eastern relies on our prior holding in *Foster v. Chesapeake Ins. Co.*, Ltd. 933 F.2d 1207 (3d Cir. 1991), in which we reviewed a similar contractual provision in the context of diversity jurisdiction.[16]

Noting that Congress had made clear its intent that foreign states and instrumentalities of foreign states shall have the right to have civil litigation decided in federal court under the FSIA, the district court concluded that a forum selection clause, by which a defendant foreign state purports to accede to jurisdiction in either federal or state court, does not preclude removal to federal court. (Citing *Proyecfin de Venezuela, S.A. v. Banco Industrial de Venezuela, S.A.*, 760 F.2d 390 (2d Cir. 1985) (forum selection clause which places jurisdiction in either federal or state court is not waiver of foreign sovereign's § 1441(d) right to remove)). Assuming for purposes of argument that

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[15] The service of suit clause in question provides:

> . . . Underwriters hereon, at the request of the Assured, will submit to the jurisdiction of any Court of competent jurisdiction within the United States and will comply with all requirements necessary to give such Court jurisdiction and all matters arising hereunder shall be determined in accordance with the law and practice of such Court.

[16] The issue of waiver is the only one remaining on rehearing. The district court dispelled the other issues raised by Texas Eastern, including its assertion that because ICI's interest in the case is allegedly *de minimis*, it should have been precluded from removing the case to federal court. The district court held that ICI clearly has a potential liability as an excess insurer of at least several million dollars, and even if its monetary interest in the case were *de minimis*, it retained the express right to remove the case to federal court under § 1441(d). The district court also found that ICI had timely removed the case to federal court.

the right to remove could be contractually waived, the district court held that, at the very least, such a waiver must be express and unambiguous in the context of the FSIA. Not finding this, the district court denied the motion of Texas Eastern to remand the action to the state court of Texas.

In examining the nature of the service of suit clause in question and its efficacy in depriving ICI of its § 1441(d) right to remove in *Texas Eastern*, we are again obliged to take cognizance of the policy imperatives of the FSIA. We find those imperatives absent in *Foster,* the case upon which Texas Eastern relies. It is true that in *Foster* we construed a forum selection clause in a reinsurance agreement as a waiver of the reinsurer's right to remove. But in *Foster*, a diversity of citizenship breach of contract case, we also explicitly noted that the FSIA poses unique considerations that might warrant a different conclusion. 933 F.2d at 1217-18 n.15. In an extensive footnote, we contrasted the diversity context of *Foster* with the FSIA removal context of *In re Delta American Re Ins. Co.*, 900 F.2d 890 (6th Cir.), *cert. denied,* 498 U.S. 890 (1990), which held that contractual waiver of the § 1441(d) right to remove, if it is to be recognized, must be clear and unequivocal. *Id.* at 894. Although waiver of a § 1441(d) right of removal was not an issue in *Foster,* we acknowledged *In re Delta's* reliance on the peculiar purposes of the FSIA, which are best served by a uniform body of law developed in federal court, and the purpose of § 1441(d) in particular, which is to give the defendant foreign state the unqualified right to remove any civil action brought against it in state court. *See also Teledyne, Inc. v. Kone Corp.*, 892 F.2d 1404, 1409 (9th Cir. 1989) (generally applicable rules of removal do not apply to the uniquely expansive § 1441(d)).

We concur with our sister circuits which give an expansive interpretation of the nature of the right to remove under § 1441(d). Given Congress' unusually strong preference for adjudication of claims against foreign states in the federal court system, we hold that it would contravene strong public policy to permit a less than absolutely unequivocal contractual provision to divest a federal district court of FSIA subject matter jurisdiction. While the FSIA does not confer exclusive jurisdiction in the federal courts and does not explicitly limit a foreign state's ability to waive its right to remove, the district court's power to remand based on breach of a contractual forum selection clause is doubtful where, as here, the clause may be construed as nothing more than a waiver of the right to contest *in personam* jurisdiction. *See Proyecifin*, 760 F.2d at 397. Thus, our holding in *Foster* is inapplicable in the FSIA context. A remand in this case would be unreasonable, and hence the purported contractual waiver is not enforceable. *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 15, 92 S. Ct. 1907, 32 L. Ed. 2d 513 (1972) (forum selection clause is binding unless enforcement is unreasonable, unfair or unjust).

Moreover, we note that ICI was not a "foreign state" within the meaning of FSIA at the time ICI subscribed the policies at issue. Thus, ICI at the time it entered into the contracts did not have an absolute right of removal under § 1441(d) to waive, and did not conduct its contract negotiations with the effect of the forum selection clause on a § 1441(d) right of removal in mind. The purported waiver was negotiated strictly between private parties. The foreign sovereign was not a party to the original contract and did not negotiate the original terms. Inasmuch as ordinary principles of contract interpretation apply here, the fact that the forum selection clause was not the subject of negotiations between Texas Eastern and the foreign state

militates against a finding of waiver. Under these circumstances, the service of suit clause does not abrogate ICI's absolute right to remove under § 1441(d). The structure and purpose of the FSIA, as well as ordinary principles of contract interpretation, support the district court's exercise of subject matter jurisdiction and its denial of Texas Eastern's motion for remand.

III.

We will affirm the district court's exercise of jurisdiction in each of the three consolidated actions that are the subject of this opinion. The substantive questions presented in these three cases were decided as to all parties in the opinion of the district court granting summary judgment against Texas Eastern, dated July 9, 1992, which we will affirm in a separate opinion filed contemporaneously with this one.

In sum, in our companion opinion which will be filed today, we affirm the judgment of the district court as to Texas Eastern's liability in all three cases. *The Fidelity & Casualty Co. of New York v. The Texas Eastern Transmission Corp.*, 15 F.3d 1249 (3d Cir. 1994). For the sake of completeness and for the purpose of appropriate cross reference, we reiterate the affirmance of that judgment here. After rehearing, we hold that the judgments of the district court as to subject matter or personal jurisdiction in *Associated Electric & Gas Insurance Services, Ltd. v. Texas Eastern Transmission Corp. et al., The Fidelity & Casualty Co. of New York v. Texas Eastern Transmission Corp.* and *Texas Eastern Transmission Corporation v. Fidelity* and *Casualty Company of New York et al.* will be affirmed in all respects.

ALITO, *Circuit Judge*, dissenting: (Dissent #1 of 2)

This case was originally decided by an unpublished opinion filed in May 1993. For two reasons, I dissented in part. First, I believed that the district court, ruling prior to our decisions in *Foster v. Chesapeake Insurance Co.*, 933 F.2d 1207 (3d Cir.), *cert. denied*, 112 S. Ct. 302, 116 L. Ed. 2d 245 (1991), and *Employers Insurance of Wausau v. Crown Cork & Seal Co.*, 942 F.2d 762 (3d Cir. 1991), had erroneously rejected TETCO's argument that subject matter jurisdiction was lacking in two of the three civil actions that were before the court — the *Texas Eastern* and *AEGIS* actions. Second, I believed that the district court's grant of summary judgment in favor of F & C in the third action — the *F & C* action — should be reversed in part. (My views on this latter issue are set out in my partial dissent from the other opinion that the panel majority has filed in this case).

On June 11, 1993, TETCO filed a petition for rehearing and a suggestion for rehearing *in banc*, contending that the district court lacked jurisdiction in the *Texas Eastern* and *AEGIS* cases. On August 18, 1993, an order granting panel rehearing was issued. After receiving supplementary briefing on the jurisdictional questions and after reargument, the panel majority has reached precisely the same conclusion as it did before, albeit in some respects for different reasons. I remain in disagreement with the majority on these jurisdictional questions, and I therefore respectfully dissent.

As noted, three civil actions were before the district court. The first case, the *F & C* action, was originally filed in the United States District Court for the Northern District of Texas, with federal jurisdiction predicated on diversity of citizenship. This is the only one of the three actions in which I think federal jurisdiction was present. The second

case, the *Texas Eastern* case, was filed in state court in Texas and subsequently removed (improperly, in my view) to the United States District Court for the Southern District of Texas. The third case, the *AEGIS* case, was filed in the United States District Court for the Eastern District of Pennsylvania, with federal jurisdiction based (wrongly, I believe) on 28 U.S.C. § 1330(a). Presumably because of the pendency of the *AEGIS* case in the Eastern District of Pennsylvania, the Judicial Panel on Multidistrict Litigation transferred the other two actions to that district and consolidated all three cases for purposes of pretrial proceedings. In September 1988, the district court rejected TETCO's challenges to the existence of federal jurisdiction in the *Texas Eastern* and *AEGIS* cases. Several years later, in a single order bearing the multi-district litigation docket number assigned to the consolidated cases, the district court granted summary judgment against TETCO, and the current appeal followed. It was by this route — based from the start on erroneous jurisdictional premises — that these cases involving difficult, unsettled, and controversial questions of Texas insurance law, found their way to our court.

I will discuss, in turn, the jurisdictional questions presented in each of the three actions that were before the district court, but I will do so in the opposite order from that used by the majority. I have chosen this order, not for sheer contrariness, but because my discussion of the *F & C action* can best be understood after I have addressed the other two cases.

I.

The *Texas Eastern* Case.

As I have noted, TETCO, preferring to litigate in the Texas state courts, originally filed this action in Harris

County, Texas, against its primary carrier, F & C, and its many excess carriers, including the Insurance Company of Ireland ("ICI"). ICI was a private entity when it entered into its insurance contract with TETCO, but "[w]hen financial difficulties threatened in 1985, the Irish government moved to preserve the company. Sealuchais Arachais Teoranta, a holding company created by the Irish Parliament and controlled by the Irish Minister for Industry, Trade, Commerce, and Tourism, acquired all of ICI's shares. With financial stability, its shares are to revert to the original shareholders." *Mobil Corp. v. Abeille General Insurance Co.*, 984 F.2d 664, 665 (5th Cir. 1993). Contending that these developments made it a "foreign state" within the meaning of 28 U.S.C. § 1603,[1/] ICI then removed this entire action to the United States District Court for the Southern District of Texas.

Assuming that ICI falls within 28 U.S.C. § 1603's definition of a "foreign state," I nevertheless believe that this removal was improper and that federal jurisdiction was lacking because the insurance contract between TETCO and ICI contained a clause featuring language that our court has already construed as a waiver of the right to remove. The clause in the TETCO-ICI contract stated that if ICI failed to

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1/ Under 28 U.S.C. § 1603(a) and (b), the term "foreign state" includes any entity

(1) which is a separate legal person, corporate or otherwise, and

(2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and

(3) which is neither a citizen of a State of the United States as defined in section 1332(c) and (d) of this title, nor created under the laws of any third country.

pay any TETCO claim, ICI would, "at the request of the Insured," "submit to the jurisdiction of any court of competent jurisdiction within the United States" and would "comply with all requirements necessary to give such Court jurisdiction." In *Foster v. Chesapeake Insurance Co.*, *supra*, one insurance company, Chesapeake, agreed to a virtually identical clause in a contract with another insurance company, Mutual Fire. When the rehabilitator appointed to marshal Mutual Fire's assets later sued Chesapeake in state court, Chesapeake removed the action based on diversity of citizenship. Holding that Chesapeake had waived its right to remove, we wrote as follows:

> [B]y consenting to "*submit*" to "*any court*" of competent jurisdiction "*at the request of the Company*," and to comply with all requirements necessary to give "*such court*" jurisdiction, Chesapeake agreed to go to, *and stay in,* the forum chosen by Mutual Fire.

Foster, 933 F.2d at 1216-17 (emphasis in original). In light of this holding, the virtually identical clause in the TETCO-ICI contract must be construed in the same way.

Although the majority tries to distinguish *Foster* on the ground that *Foster* involved removal based on diversity, rather than the Foreign Sovereign Immunities Act (FSIA), I find that effort unconvincing. The majority states:

> Given Congress' unusually strong preference for adjudication of claims against foreign states in the federal court system, we hold that it would contravene strong public policy to permit a *less than absolutely unequivocal contractual*

> *provision* to divest a federal district court of FSIA subject matter jurisdiction.

Maj. Op. #1, at 1243 (emphasis added). This argument seems to fly in the face of *Foster*. Immediately after noting that *In Re: Delta Insurance Co.*, 900 F.2d 890 (6th Cir.), *cert. denied*, 498 U.S. 890 (1990), had held that a waiver of the right to remove under the FSIA must be clear and unequivocal, the *Foster* panel wrote:

> *[W]e do not see why contractual waivers of the right to remove must be clear and unequivocal* . . . .
>
> *We* think the "clear and convincing" standard so stringent as to be contrary to the right of parties to contract in advance regarding where they will litigate. A court simply should determine contractual waiver of the right to remove using the same benchmarks of construction and, if applicable, interpretation as it employs in resolving all preliminary contractual questions. Indeed, inasmuch as the determination of whether there is a waiver of the right of removal to be derived from a forum selection clause will at least in some cases, such as here, be a matter of construction and thus of law, it seems anomalous to speak of a "clear and unequivocal" standard for we simply make plenary determinations of legal issues.

933 F.2d at 1218 n.15 (emphasis added). I do not believe that the majority's decision in this case can be reconciled with this passage.

Moreover, even if such reconciliation were possible, I would find the majority's position unacceptable, for I cannot understand why "foreign states," when they choose to enter into contracts, should have the benefit of especially favorable rules of contract construction or interpretation. Are "foreign states" unable to afford competent lawyers to draft and review their contracts and thereby insure that the removal rights conferred by 28 U.S.C. § 1441(d) are not inadvertently compromised?

In any event, even if it were appropriate to apply such a rule to contracts signed by a foreign state, it simply makes no sense to apply that rule to the TETCO-ICI contract, since ICI was not a "foreign state" when that contract was formed. When TETCO entered into its agreement with ICI, it contracted for (and presumably paid for) ICI's agreement not to exercise any of the rights it then possessed to resist the jurisdiction of any court of competent jurisdiction in the United States. I do not think that TETCO should lose the benefit of this bargain simply because the Irish government chose to acquire ICI's assets. Nor do I think that TETCO should be penalized for failing to secure from ICI an agreement specifically stating that, if ICI should subsequently become a "foreign state," it would not exercise the special removal rights that such states possess. We can properly demand that parties exercise prudent foresight; we cannot require clairvoyance.

II.

The *AEGIS* Action.

Two of TETCO's excess insurers, Associated Electric & Gas Insurance Services, Ltd. (AEGIS) and National Surety Corp. (NS), filed this action in the United States District Court for the Eastern District of Pennsylvania

against TETCO, F & C, and TETCO's other excess carriers, including ICI. Relying on ICI's status as a defendant, the complaint alleged that jurisdiction was present based on 28 U.S.C. § 1330(a), which confers jurisdiction over a "civil action against a foreign state."

In its initial brief on appeal, TETCO argued that this action was not in reality against a foreign state. TETCO contended that the "primary issue" test adopted in *Employers Insurance of Wausau v. Crown Cork & Seal Co.*, *supra*, should be applied, that the realignment of the parties was therefore required, and that ICI should be realigned as a plaintiff. After such realignment, TETCO argued, jurisdiction under 28 U.S.C. § 1330(a) would be lacking because the action would not be one "*against* a foreign state." TETCO Br. at 67-68 (emphasis added).

In response, the carriers did not argue that the "substantial conflict" test or any other lesser standard should be applied to determine whether ICI's interests were adverse to those of the other carriers. Nor did the carriers even hint that there was any real conflict between ICI and the other carriers. Instead, the carriers contended that "[r]ealignment to test subject matter jurisdiction is not appropriate where jurisdiction is based on the FSIA. Rather, it is an antidote to artificial maneuvers by parties to create diversity jurisdiction." Appellees' Joint Br. at 66. Alternatively, the carriers argued that, if the parties were realigned, one of the following two realignments should be chosen: "TETCO as plaintiff and the Carriers as defendants" or "all Carriers plaintiffs and TETCO a defendant." *Id.* at 66, 67. Tellingly, both of these realignments place all of the carriers, including ICI, on the same side.

In its initial unpublished opinion, the panel majority agreed with the carriers that realignment need not be

considered. The panel described realignment as "a creature of diversity jurisprudence" and concluded that "application of realignment to Immunities Act jurisdiction would not serve any purpose." Op. at 7. Now, however, the majority states:

> [I]t is self-evident that Congress conditioned its conferral of jurisdiction on the substantive party alignment of any purported *FSIA* action. Thus we are obliged to ascertain the real adversity of interest between AEGIS and ICI in the *AEGIS* case and to realign them according to their substantive interests before recognizing section 1330 jurisdiction.

Maj. Op. #1, at 1239. Nevertheless, the majority again reaches the conclusion that the district court had jurisdiction over the *AEGIS* action under 28 U.S.C. § 1330(a). The majority reasons that this provision requires a lesser degree of adversity than is needed in diversity cases. Rejecting the "primary issue" test that our court has adopted in diversity cases, the majority holds that no more than a "substantial conflict" is necessary and finds that that test is satisfied here. The majority bases this conclusion on (1) the fact that the AEGIS complaint sought, among other things, a declaration of the plaintiffs' rights with respect to the carriers named as defendants, including ICI, and (2) a statement made by the carriers' counsel at oral argument. Maj. Op. #1, at 1241-1242. I disagree with this approach.

First, I question whether we should abandon the "primary issue" test simply because federal jurisdiction is invoked under 28 U.S.C § 1330(a) rather than 28 U.S.C. § 1332(a)(1). Particularly if the "substantial conflict" test can be satisfied with the type of showing that the majority

finds sufficient, I fear that that test may permit the unwarranted evasion of federal jurisdictional requirements. Second, even if the "substantial conflict" test is to be applied, I am not willing to hold that a "substantial conflict" exists in this case based on the facts that the majority cites. Surely, a "substantial conflict" cannot be found solely because that the complaint requests a declaration of AEGIS's and NS's rights with respect to ICI. Nor do I think that we should base our decision solely on the remarks of the carriers' attorney at oral argument. I certainly recognize, as the carriers' attorney pointed out, that the interests of the primary carrier, F & C, might under some circumstances become adverse to those of the excess carriers and that the interests of excess carriers at "different levels" might become adverse. The critical question here, however, is whether there was in fact at least a "substantial conflict" between, on the one hand, two particular excess carriers (AEGIS and NS) and, on the other hand, another particular excess carrier (ICI). This question cannot be decided without analyzing the actual terms of the relevant insurance contracts. The parties have never provided us with any such analysis, and I do not think that we should attempt to perform such analysis on our own at the panel rehearing stage. Therefore, at the very least, I think that a remand to the district court is needed so that an appropriate analysis can be undertaken and so that the disposition of this question can be based on facts rather than supposition.

III.

The *F & C* Action.

This action was filed by F & C in the United States District Court for the Northern District of Texas against TETCO, with jurisdiction based on diversity of citizenship.

There is no question that the district court had jurisdiction with respect to this action, but it is now hotly disputed whether the excess insurance carriers were or could properly be made parties to this action. F & C did not name the excess insurers as parties — and F & C could not have named many of them without destroying federal jurisdiction, since they share common citizenship with TETCO. As noted, however, the excess carriers were named as parties in the *Texas Eastern* and *AEGIS* actions. After those cases had been consolidated with the *F & C* action and after TETCO's jurisdictional challenges in the *Texas Eastern* and *AEGIS* actions had been rejected, TETCO filed counterclaims against the excess insurers in the *F & C* case, but TETCO never served the excess carriers with summonses, and many of them asserted the absence of personal jurisdiction as a defense. For the most part, however, it appears that the parties and the district court paid little if any attention to the question whether the excess insurers were parties in the *F & C* case as opposed to the other two consolidated cases.

It was not until TETCO petitioned for rehearing that the parties paid any significant attention to the question whether the excess insurers had been made parties in the *F & C* case. Then, after panel rehearing was granted, both sides advanced precisely the opposite of the arguments that one would have expected them to make when the counterclaims were filed. TETCO offered a long list of reasons why its own counterclaims were defective: the counterclaims were never served, and the excess insurers did not waive their objections to personal jurisdiction; the counterclaims were improper under Fed. R. Civ. P. 13(h) and, in any event, the district court never decided whether, in the exercise of its discretion, it would permit the excess insurers to be joined under that provision; and finally, since there was no independent federal jurisdictional basis for TETCO's

counterclaims against the excess insurers, the district court could not, under *Finley v. United States*, 490 U.S. 545 (1989), exercise jurisdiction over them. The carriers responded with an equally lengthy list of reasons why the excess insurers had properly been made parties. Agreeing with the carriers, the majority rejects all of TETCO's arguments. Among other things, the majority finds that the excess insurers waived their objections to personal jurisdiction by litigating in the district court, and the majority adopts a narrow (and, to my mind, questionable) interpretation of *Finley*.

I think it is inadvisable for the panel to delve into these questions at this juncture. For example, I would not, at the rehearing stage, decide whether the excess insurers participated in the *F & C* case (as opposed to the other two cases) so as to be deemed to have waived their objections to personal jurisdiction; this is a fact-bound question never addressed by the district court. Nor would I rush to decide whether, despite *Finley*, the district court could exercise subject matter jurisdiction over the counterclaims.

Beginning in September 1988, when the district court rejected TETCO's jurisdictional challenges to the *Texas Eastern* and *AEGIS* actions, the proceedings in the three consolidated cases went forward on the premise that the court had jurisdiction in all three actions. Hence, when the district court granted summary judgment against TETCO, it issued a single order bearing the multi-district litigation docket number assigned to all three consolidated cases. Since I believe that the district court lacked jurisdiction in two of those actions, I would vacate that order and remand the *F & C* case to the district court. The district court could then, in the first instance, rule on whatever arguments the parties chose to pursue. If necessary, the district court could also, in the first instance, decide the fact-bound

question whether the excess insurers waived any objections to personal jurisdiction in the *F & C* case as a result of participating in it. Until the district court has ruled, however, I do not think that our court should consider the long list of questions — some highly artificial, some fact-bound, and some legally difficult — that the parties advanced with respect to these counterclaims after panel rehearing was granted.

A True Copy:
Teste:

Clerk of the United States Court of Appeals
for the Third Circuit

Filed January 10, 1994

OPINION 2 OF 2

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 92-1638

IN RE: TEXAS EASTERN TRANSMISSION CORP. PCB CONTAMINATION INSURANCE COVERAGE LITIGATION
(MDL No. 764)

THE FIDELITY & CASUALTY CO. OF NEW YORK

v.

THE TEXAS EASTERN TRANSMISSION CORP.
[D.C. Civil No. 88-05039]

ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD.; NATIONAL SURETY CORPORATION

v.

TEXAS EASTERN TRANSMISSION CORPORATION; FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK; CERTAIN UNDERWRITERS AT LLOYDS OF LONDON, INCLUDING THE INSURANCE COMPANY OF IRELAND; AETNA CASUALTY AND SURETY COMPANY; AMERICAN HOME ASSURANCE COMPANY; BOSTON OLD COLONY INSURANCE COMPANY; CONTINENTAL CASUALTY INSURANCE COMPANY; FIRST STATE INSURANCE COMPANY; HIGHLANDS INSURANCE COMPANY; THE HOME INSURANCE COMPANY; INSURANCE COMPANY OF NORTH AMERICA; INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA; INTERNATIONAL INSURANCE COMPANY; LEXINGTON INSURANCE COMPANY; MIDLAND INSURANCE COMPANY; MUTUAL MARINE INSURANCE

COMPANY; PRUDENTIAL REINSURANCE COMPANY; RANGER INSURANCE COMPANY; REPUBLIC INSURANCE COMPANY; STONEWALL INSURANCE COMPANY; PENNSYLVANIA INSURANCE GUARANTY ASSOCIATION; UNITED STATES OF AMERICA; UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
(D.C. Civil No. 88-02126)

TEXAS EASTERN TRANSMISSION CORPORATION

v.

FIDELITY AND CASUALTY COMPANY OF NEW YORK; ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD.; AETNA CASUALTY AND SURETY COMPANY; AMERICAN HOME ASSURANCE COMPANY, a/k/a AMERICAN HOME INSURANCE COMPANY; BOSTON OLD COLONY INSURANCE COMPANY; CIGNA INSURANCE COMPANY; CONTINENTAL CASUALTY COMPANY; EMPLOYERS MUTUAL CASUALTY COMPANY; FIRST STATE INSURANCE COMPANY; HIGHLANDS INSURANCE COMPANY; THE HOME INSURANCE COMPANY; THE INSURANCE COMPANY OF NORTH AMERICA; INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA; INTERNATIONAL INSURANCE COMPANY; LEXINGTON INSURANCE COMPANY; MIDLAND INSURANCE COMPANY; NATIONAL SURETY CORPORATION; PRUDENTIAL REINSURANCE COMPANY; RANGER INSURANCE COMPANY; REPUBLIC INSURANCE COMPANY; STONEWALL INSURANCE COMPANY; UNITED STATES FIRE INSURANCE COMPANY; CERTAIN UNDERWRITERS AT LLOYD'S, LONDON and CERTAIN LONDON MARKET INSURANCE COMPANIES
(D.C. Civil No. 88-05707)

Texas Eastern Transmission Corporation,

Appellant

Appeal from the United States District Court
for the Eastern District of Pennsylvania

Argued
April 7, 1993

OPINION OF THE COURT

MANSMANN, *Circuit Judge*.

Preliminary Note

Three cases filed in three courts were consolidated for trial in the district court from whose combined judgments these appeals have been taken at No. 92-1638. This opinion addresses only one facet of these cases — the liability of Texas Eastern Transmission Corp. as adjudicated by the district court in *Fidelity & Casualty Co. of New York v. The Texas Eastern Transmission Corp.*, (hereinafter the "F & C" action) originally filed in the Northern District of Texas, *Texas Eastern Transmission Corp. v. Fidelity and Casualty Co. of New York et al.*, (hereinafter the "*Texas Eastern*" action) originally filed in a Texas state court and later removed to the Southern District of Texas, and *Associated Electric & Gas Insurance Services, Ltd. et al. v. Texas Eastern Transmission Corp et al.* (hereinafter the "*AEGIS*" action) filed in the Eastern District of Pennsylvania. All three cases were later assigned by the Multi-District Litigation Panel to the district court below.

On April 7, 1993, we heard argument on the appeal of Texas Eastern Transmission Company from the judgment of

the district court, in a multi-district litigation, declaring that Texas Eastern's insurance carriers (the "Carriers") were not liable for damages arising out of Texas Eastern's discharge of PCB-laden oils into the environment. Our unreported opinion, affirming the district court's judgment, was filed on May 28, 1993. We vacated that opinion on January 6, 1994. This opinion in effect reinstates the discussion on liability set forth in our previous not-for-publication opinion.

We deem it necessary to write separate opinions because Texas Eastern Transmission Corp. petitioned for rehearing in only two of the cases — *Texas Eastern* and *AEGIS* — and only on the subject matter jurisdiction issue. We ordered panel rehearing in those two cases only, stayed our mandate in all three cases and ordered oral re-argument of the question of subject matter jurisdiction in the two cases. Our companion opinion discusses subject matter jurisdiction in the cases that were reheard and also the question of jurisdiction in *F & C* because jurisdiction in that case was indirectly put to question in the rehearing arguments. This opinion addresses once again the subject of Texas Eastern's liability in all three cases.

Texas Eastern Transmission Corporation claimed that its comprehensive general liability insurance carriers (the "Carriers") must pay for damages associated with the cost of removing PCBs that present a danger of polluting the property of third parties. The district court granted summary judgment against Texas Eastern on the theory that Texas Eastern provided prejudicially late notice of its claim to the Carriers. We will affirm in the case of *Fidelity Casualty Co. of New York v. Texas Eastern Transmission Co.*, D.C. Civ. No. 88-05039 (E.D. Pa.).

I.

The relevant facts, which appear in great detail in the district court's opinion, may be summarized as follows.

Until the early 1970s, Texas Eastern used a toxic, PCB-laden lubricant in compressor stations along a pipeline that stretched 9,500 miles, from Texas to New York. The lubricant co-mingled with other toxic fluids in the pipeline, and Texas Eastern discharged those fluids into the environment, either by venting them into the air during start-up or shut-down, or by discharging them into earthen pits, which occasionally overflowed. Texas Eastern would also occasionally spray fluids from the pits to kill weeds or to control dust.

As early as 1972, the lubricant's manufacturer informed Texas Eastern that the lubricant contained toxic PCBs. Throughout the late 1970s and early 1980s, Texas Eastern became increasingly aware that PCBs were entering the environment via the pipeline fluid. The district court determined that, taking all inferences in favor of Texas Eastern, a genuine issue of material fact existed as to whether Texas Eastern knew between 1970 and December 1986 that PCBs were present in the pipeline fluid and that the PCBs could migrate, via the pipeline fluid, onto the property of third parties. That issue was critical because such knowledge would trigger Texas Eastern's obligation to notify Carriers of an insurable "occurrence" under the relevant insurance policies.

Employing the correct summary judgment standard, the district court determined that although a rational factfinder could conclude that Texas Eastern knew PCBs were migrating to the property of third parties as early as 1972,

December of 1986 was the latest possible date a jury could conclude that Texas Eastern discovered that PCBs were migrating onto the property of third parties. The district court based its determination in part on Texas Eastern's concession that in December, 1986, a preliminary report commissioned by Texas Eastern gave it reason to know that PCBs were migrating off-site.

As we review in more detail below, between December, 1986, and August, 1987, Texas Eastern entered into at least one consent decree and negotiated in earnest with the Environmental Protection Agency. After some months of negotiation with EPA, Texas Eastern notified the Carriers of a potential occurrence giving rise to a claim. The cost of clean-up is now estimated at $750 million.

Fidelity and Casualty, Texas Eastern's primary carrier, brought its case in the Northern District of Texas premised on diversity jurisdiction, seeking a declaratory judgment that it was not liable under its policy for the claims. Associated Electric & Gas Insurance Services, Ltd. ("AEGIS") and National Surety Corporation, other carriers of Texas Eastern, brought a second suit against Texas Eastern and all of the remaining carriers in the Eastern District of Pennsylvania. Federal subject matter jurisdiction in the *AEGIS* action was premised on the Foreign Sovereign Immunities Act. Texas Eastern brought a third state-court action against all the carriers, later removed to the Southern District of Texas also on the basis of the Immunities Act. Because we address whether Immunities Act jurisdiction was proper in a separate opinion, that issue will not be discussed here.

In an extensive opinion, the district court determined that summary judgment should be entered against Texas Eastern on the ground that its delay in providing notice to

the Carriers was unreasonable and prejudicial as a matter of law. *In re Texas Eastern Transmission Corporation PCB Contamination Insurance Coverage Litigation*, No. MDL-764 (E.D. Pa. July 9, 1992).

We exercise plenary review of the district court's grant of summary judgment, applying "the same test the district court should have used initially." *Goodman v. Mead Johnson & Co.*, 534 F.2d 566, 573 (3d Cir. 1976), *cert. denied*, 429 U.S. 1038 (1977). *See generally Celotex Corp. v. Catrett*, 477 U.S. 317 (1986); *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242 (1986); *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986).

The district court clearly had diversity jurisdiction over one of the three cases that constitute this multi-district litigation. *Fidelity & Cas. Co. v. Texas Eastern*. The other two cases, *Associated Electric & Gas Ms. Svs. v. Texas Eastern*, No. 88-021267 ("*AEGIS*") and *Texas Eastern v. Fidelity & Cas. Co.*, No. 88-05707, are premised on jurisdiction under the Foreign Sovereign Immunities Act, and they are the subject of an opinion filed contemporaneously with this one. We have jurisdiction of a final decision of the district court. 28 U.S.C. § 1291.

II.

In determining that late notice relieved the Carriers[1/] of any obligation under the contracts, the district court reached three central conclusions. First, Texas Eastern's

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1/ Although we decide here only the diversity case involving Fidelity and Casualty, D.C. Civ. No. 88-05039, the Carriers submitted a joint brief, and so we refer to Fidelity & Casualty's position generically as the Carriers' position.

duty to inform the carriers of an "occurrence" accrued not later than December of 1986. Second, Texas Eastern provided unreasonably late notice to the Carriers eight or nine months later, in August of 1987. Third, the unreasonably late notice prejudiced the Carriers. Although Texas Eastern challenges all three conclusions, only the third, regarding prejudice, merits some discussion.

A.

To predict the standard of prejudice applied under Texas law, we must first review the relevant line of Texas cases. The Texas Supreme Court long adhered to the rule that an insured's delay in providing notice relieved a carrier of liability under the policy, even in the harsh case when the carrier stipulated that it had not suffered any prejudice at all. *See Members Mutual Ins. Co. v. Cutaia*, 476 S.W.2d 278 (Tex. 1972) (stating harsh rule).

In 1973, the Texas State Board of Insurance ordered that the following Amendatory Endorsement be attached to general liability policies:

> As respects *bodily injury* liability coverage and *property damage* liability coverage, unless the company is prejudiced by the insured's failure to comply with the requirement, any provision of this policy requiring the *insured* to give notice of action, *occurrence* or loss, or requiring the *insured* to forward demands, notices, summons or other legal process, shall not bar liability under this policy.

See R. at 869-72 (Order of Insurance Board).

Although "there is a paucity of authority explicating what, within the purview of the endorsement, would constitute prejudice sufficient to relieve an insurer of liability," *Kimble v. Aetna Casualty & Surety Co.*, 767 S.W.2d 846, 850 (Tex. Ct. App. 1989), at least one Texas appellate court has stated clearly that prejudice results to the insurer by "*the change in its position*" brought about by an insured's failure to notify. *Members Ins. Co. v. Branscum*, 803 S.W.2d 462, 466 (Tex. Ct. App. 1991) (emphasis added) (citing *Kimble*, 767 S.W.2d at 851). Our task, therefore, is to determine what constitutes prejudice under Texas law.

While we find helpful the change-in-position elaboration on the legal meaning of prejudice, the question remains how substantial that change in position must be before a court can conclude that, as a matter of law, a carrier has suffered prejudice. In some states, for example, courts have imposed a "substantial prejudice" standard, which requires a demonstration that an insurer *could* have either defeated a claim or settled for a smaller sum than the sum for which the insured ultimately settled. *Insurance Co. of Pa. v. Associated Int'l Ins. Co.*, 922 F.2d 516, 524 (9th Cir. 1990) (applying California law). To determine the extent of harm sufficient to constitute prejudice under Texas law, we find instructive the facts of several Texas cases.

In a number of cases, Texas courts have held that notice to a carrier after the entry of a default judgment has become final constitutes prejudice, as a matter of law, sufficient to defeat the carrier's liability under a policy. *See, e.g., Ratcliff v. National County Mut. Fire Ins. Co.*, 735 S.W.2d 955, 957 (Tex. Ct. App. 1987). *Compare Allstate Ins. Co. v. Pare*, 688 S.W.2d 680 (Tex. Ct. App. 1984) (no prejudice where insurer received papers before default and had negotiated for settlement prior to default).

Notably, the court in *Ratcliff* did not require the carrier to show that it would have or could have defended the suit successfully or reached a better settlement. We note also that in *Kimble* the court determined that prejudice existed notwithstanding that the carrier learned of the suit before the judgment became final. 767 S.W.2d at 850. Observing that opening of the judgment was uncertain, the court did not assign any burden to the carrier to show that it would have litigated the case or to explain why it did not enter the litigation. *Id.* at 850-51. Similarly, in *Branscum*, the court held that prejudice resulted when a carrier learned of a final default judgment, notwithstanding that the carrier had had actual knowledge of the underlying accident, had engaged in settlement negotiations, and had known of an impending suit. 803 S.W.2d at 463-64.

These cases demonstrate that the Texas courts do not utilize a "substantial prejudice" standard and do not impose on carriers the burden of explaining non-action such as failure to obtain papers in an impending suit. Indeed, the court in *Branscum* stated unequivocally that "application of a 'substantial' prejudice standard is erroneous." *Branscum*, 803 S.W.2d at 467.

Upon review of the Texas caselaw discussed above, we predict that the Texas courts would apply a standard of prejudice somewhat lower than "substantial prejudice" and closer to a concept of permitting carriers to deny coverage when there is evidence of change in position adverse to a carrier's interest. *See Branscum*, 803 S.W.2d at 466; *Kimble*, 767 S.W.2d at 851. Although the change must obviously be material under this standard of prejudice, the carrier need not show that the change is irreversible in order to demonstrate that prejudice has resulted. *E.g.*, *Kimble*, 767 S.W.2d at 851 (holding of prejudice, notwithstanding carrier's rejection of option to petition to

vacate default). With these decisions in mind, we turn now to a review of the district court's conclusion.

B.

In concluding that the Carriers were prejudiced by Texas Eastern's delay of at least eight months in providing notice, the district court assumed without deciding that prejudice was a necessary element to the Carrier's defense of late notice. The district court then examined the events that the parties do not dispute took place between December, 1986 (the latest date that the duty to notify accrued), and late August, 1987 (the date Texas Eastern actually gave notice to the Carriers).

On December 15, 1986, several days after it had received from its broker a comprehensive list of carriers and notice provisions, Texas Eastern proposed a cleanup plan to the EPA. Op. at 149. (Four days later, Texas Eastern met with EPA officials to discuss the establishment of a framework for future discussions on remediating contaminated on-site areas on Texas Eastern's system. R. at 1036-37. Within a month, Texas Eastern had furnished EPA with a summary of a preliminary environmental report and a "Summary of Dioxin Sampling and Analysis." R. at 1036, ¶ 375-76.)[2/] As the district court noted:

> By this time, Texas Eastern was committed to remediating the PCB contamination in its unlined earthen pits and the only material dispute between

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[2/] Here and in the following paragraphs, we have noted parenthetically specifics to which the district court did not refer expressly.

> Texas Eastern and EPA was the extent of the cleanup and the form of the agreement which would be required.

Op. at 149.

In February of 1987, at approximately the same time that the Houston Chronicle published an article detailing Texas Eastern's PCB-related problems, Texas Eastern considered giving notice, but did not. Op. at 150-51. On March 17, Texas Eastern testified before a United States Senate Subcommittee regarding its PCB problem and the status of its *already* ongoing settlement discussions with EPA. And in April, settlement negotiations became intensive, with EPA insisting that cleanup levels be based on EPA's "risk assessments" and with EPA demanding that Texas Eastern consider off-site contamination and enter into formal negotiations to discuss specific cleanup demands. Op. at 151-52. It was at this point that Texas Eastern entered into a consent decree with the Commonwealth of Pennsylvania. Op. at 172. (That decree contained numerous stipulations of fact, and it established testing and monitoring methodologies and schedules that Texas Eastern would follow. R. at 4968.)

By mid-August, significant and extensive negotiations had already taken place, as indicated by the contents of a letter dated August 18 from Carol Dinkins, Texas Eastern's negotiator, to EPA. Op. at 152. The letter summarizes fifteen major issues for inclusion in a comprehensive settlement, among them Texas Eastern's proposal to pay substantial civil penalties and oversight costs. R. at 808-809. (The letter also discloses Texas Eastern's bargaining position: "Texas Eastern proposes to undertake a far greater commitment of work at many more sites than EPA has ever seen any party voluntarily step forward to

work out. . . ." R. at 809.) A few days later, Texas Eastern mailed its notice of claim, dated August 19, 1987, to the Carriers.

With respect to these events, the district court held:

> By the time Texas Eastern gave notice, remedial efforts, testing and monitoring had begun, and schedules and methodologies to characterize the sites had been established. Most importantly, Texas Eastern had already presented to EPA its proposed settlement terms, and thus completely destroyed any meaningful opportunity for the Carriers to shape negotiations with EPA. The record makes it abundantly clear that Texas Eastern never wanted the Carriers to interfere with what was a carefully negotiated settlement with EPA and waited until the settlement was substantially agreed upon before providing any notice to the Carriers.

Op. at 172-73.

Texas Eastern does not dispute that, by August 19, 1987, the Carriers had lost an opportunity to participate initially in "remedial efforts, testing, . . . monitoring, and [establishment of] schedules and methodologies." Op. at 172-73. Indeed, Texas Eastern's assertion that insurers do not generally get involved in environmental investigations and negotiations is without record support. *See* Br. for Appellant at 31; Rep. Br. for Appellant at 3 n.3. Nor does Texas Eastern dispute that, as of August 18, 1987, at least one day before notice was provided, Texas Eastern had *already* disclosed its bargaining position to EPA, or, in the

parlance of poker players, tipped its hand by, for example, proposing to pay a substantial civil penalty and to undertake a voluntary cleanup far greater than EPA had ever seen. Under the law of Texas, these undisputed facts alone justify the district court's holding because they indicate prejudice resulting from a material change in the Carriers' bargaining position. *See Branscum*, 803 S.W.2d at 466. Because the above changes resulted in prejudice, we need not address the Carriers' additional arguments that prejudice resulted from Texas Eastern's waiver of rights against the United States and from Texas Eastern's renewal of its insurance contracts prior to notifying the Carriers of the claim.

C.

Because prejudice to the carriers flows from the *ex parte* participation of Texas Eastern in its field investigations and in its negotiations, it follows that Texas Eastern's disputations that "there was no 'done deal' between Texas Eastern and EPA in August, 1987" are not persuasive. The district court did not say that the matter was a "done deal," but that "the matter was for *all intents and purposes* . . . a 'done deal.'" Op. at 170 (emphasis added). Indeed, most, if not all, of the points in the August 18 letter found their way, in some form or other, into the final consent decree. *Compare* R. at 805 (Dinkins's letter) *with* R. at 557 (consent decree).

Moreover, Texas Eastern's assertions that the Carriers had the option of entering the negotiations after August 18, 1987, are immaterial to the issue of whether prejudice occurred *prior* to that date through a material change in position. In *Kimble*, a carrier chose not to enter litigation, even though there remained time to do so. 767 S.W.2d at 846. As the court in *Branscum* noted:

> The *Kimble* court held that prejudice results to the insurer by the change in its position brought about by the insured's failure to forward the suit papers until after the default. Prejudice results *even though the option to file a new trial is still available to the insurer*. *Kimble*, 767 S.W.2d at 851.

Branscum, 803 S.W.2d at 466 (emphasis added). By analogy, prejudice resulted here even though the option to enter negotiations was still available to the Carriers.

Texas Eastern submits one further challenge to the district court's determination of prejudice, namely, that the Carriers must show that they would have entered negotiations earlier and that they could have altered the outcome. This challenge, however, seeks to apply the "substantial prejudice" standard to the Carriers, whereas the tone and tenor of extant Texas caselaw indicates that the application of that standard would be erroneous.[3/] *See, e.g., Branscum*, 803 S.W.2d at 467.

[3/] The position of the dissent, that the carriers must demonstrate that they *would* have entered into negotiations in order to demonstrate prejudice from late notice, *see* dissent at 11, does not comport with our reading of the Texas caselaw. Moreover, the dissent's approach would inappropriately render a notice defense unavailable under Texas law any time a carrier also asserted other bona fide defenses to coverage.

For example, a carrier might refuse to defend against a battery claim on the grounds that a policy clearly limited the carrier's obligation to the defense of negligence. That carrier would never be able to meet the dissent's "actual prejudice" standard, no matter how egregious the lateness of notice.

D.

Because we have determined that the district court correctly concluded that the carriers were prejudiced, we need not address the remaining contentions of Texas Eastern.

III.

For the foregoing reasons, we will affirm the judgment of the district court as to liability of Texas Eastern in all three cases.

ALITO, *Circuit Judge*, dissenting in part: (Dissent #2 of 2)

In my dissent from the majority's separate opinion concerning the jurisdictional issues presented in this appeal, I explain why I believe that the district court lacked jurisdiction with respect to two of three actions that were before it: the *Texas Eastern* and *AEGIS* actions. That dissent also addresses the question whether TETCO's excess insurers are properly parties in the third action: the *F & C* action. In this opinion, I explain why I believe that the district court's grant of summary judgment in favor of F & C in the *F & C* action should be partially reversed.

The *F & C* action involved the availability of coverage for TETCO's PCB-related problems under a series of policies that were in effect from 1961 through 1988. All of these policies generally required TETCO to notify F & C "as soon as practicable" after becoming aware of an "occurrence" that appeared likely to trigger coverage. The policies effective on or after May 1, 1973, provide that F & C could deny coverage based on lack of timely notice

only if it suffered some degree of actual prejudice. By contrast, under the earlier policies, lack of timely notice allowed F & C to deny coverage without any inquiry into prejudice. The policies in effect from July 1, 1970, through January 1, 1981, also contain a clause excluding coverage for damage caused by pollution unless the pollution was "sudden and accidental."[1/] The earlier and later policies do not contain this pollution exclusion clause.

Because TETCO's policies with F & C provided coverage for damage to the property of others but not to TETCO's own property, the notice requirement meant, as the district court concluded, that TETCO was obligated to notify its insurers promptly upon learning that PCBs were migrating beyond its own property lines, since off-site migration was the "occurrence" likely to produce claims potentially covered by the policies.[2/] The district court

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1/ The exclusion clause reads:

> This policy does not apply . . . to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any watercourse or body of water; but this exclusion does not apply if such discharge, dispersal, release or escape is sudden and accidental.

2/ Because of my conclusion that the merits of the coverage dispute between TETCO and its excess insurance carriers were not properly before the district court, I need only consider the effect of TETCO's late notice on F & C. However, since the majority considers the question of late notice with respect to the insurance carriers as a group, and because I agree with the majority that such treatment is appropriate, I write in terms of the effect of late notice on all insurers.

held that this notice obligation accrued no later than December 1986 — the month during which TETCO received a report documenting off-site PCB migration. But even if this obligation did not arise until as late as May 1987 — when the EPA demanded cleanup measures aimed at preventing additional off-site migration — TETCO's notice in August 1987 could not reasonably be regarded as having been given "as soon as practicable." TETCO is certainly capable of moving faster than this when its own interests are at stake. Thus, I agree with the district court and the panel majority that TETCO did not comply with its notice obligation. On this basis, I agree that the district court properly granted summary judgment in favor of F & C with respect to those claims falling under the earlier policies that did not require a showing of actual prejudice.

With respect to claims under the more recent policies, however, Texas law allowed coverage to be denied because of late notice only if the insurers suffered actual prejudice. See Maj. Op. #2, Typescript at 13-16. Unlike the majority, I am convinced that summary judgment for the insurers on the issue of actual prejudice was improper. The majority correctly observes that TETCO's late notice deprived the insurers of the opportunity to participate in the settlement negotiations between TETCO and the EPA that took place during the summer of 1987. I wholeheartedly agree that these were important discussions and that the insurers suffered prejudice *if, given the opportunity, the insurers would have participated in or at least seriously considered participating in these discussions*. But what if the insurers would not have participated in these discussions or even seriously considered doing so? Could it then be said that they suffered prejudice in any meaningful sense? I do not think so.

Before holding that TETCO's claims are barred because the insurers were prejudiced, I think we should require at least some support in the summary judgment record indicating that the insurers would or realistically might have availed themselves of the supposedly valuable opportunity that they lost. There is, however, no such support — no affidavits or other support concerning (a) what the insurers would have done in this case had they received prompt notice, (b) these insurers' usual practices regarding involvement in EPA settlement negotiations in cases such as this, or (c) prevailing practices in the insurance industry as a whole in comparable cases.

In this case, although the insurers' potential liability was huge they had many promising legal defenses. Under these circumstances, it may well be that the insurers, if given prompt notice, would have summarily concluded that their best strategy was to let TETCO negotiate on its own and then to litigate any subsequent claims for coverage. This is precisely the strategy that the insurers did adopt after they received TETCO's notice. Without anything in the summary judgment record to show that the insurers would not have taken this approach had they received notice more promptly, I do not think that summary judgment on this issue was proper.

While I cannot agree that the insurers were entitled to summary judgment on the issue of actual prejudice, I agree that they were entitled to summary judgment with respect to some of the policies on an alternative ground cited by the district court: the presence of a pollution exclusion clause in some of the policies. According to the district court, summary judgment against TETCO was proper as to these policies because the damage caused by off-site PCB migration was not "sudden and accidental." For essentially

the reasons given by the district court,[3/] I believe that this alternative holding was correct. Accordingly, I would affirm the district court's grant of summary judgment in favor of F & C as to the policies containing both an actual prejudice requirement and this pollution exclusion clause.

In sum, I would affirm in part and vacate in part the grant of summary judgment in favor of F & C in the *F & C* case, and I would remand that case to the district court for further proceedings.

A True Copy:
Teste:

Clerk of the United States Court of Appeals
for the Third Circuit

3/ Dist. Ct. Op. at 123-37.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 92-1638

IN RE: TEXAS EASTERN TRANSMISSION CORP. PCB CONTAMINATION INSURANCE COVERAGE LITIGATION (MDL No. 764)

ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD.;
NATIONAL SURETY CORPORATION

v.

TEXAS EASTERN TRANSMISSION CORPORATION;
FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK;
CERTAIN UNDERWRITERS AT LLOYDS OF LONDON, INCLUDING THE INSURANCE COMPANY OF IRELAND;
AETNA CASUALTY AND SURETY COMPANY;
AMERICAN HOME ASSURANCE COMPANY;
BOSTON OLD COLONY INSURANCE COMPANY;
CONTINENTAL CASUALTY INSURANCE COMPANY;
FIRST STATE INSURANCE COMPANY;
HIGHLANDS INSURANCE COMPANY;
THE HOME INSURANCE COMPANY;
INSURANCE COMPANY OF NORTH AMERICA;
INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA;
INTERNATIONAL INSURANCE COMPANY;
LEXINGTON INSURANCE COMPANY;
MIDLAND INSURANCE COMPANY
MUTUAL MARINE INSURANCE COMPANY;
PRUDENTIAL REINSURANCE COMPANY;
RANGER INSURANCE COMPANY;
REPUBLIC INSURANCE COMPANY;
STONEWALL INSURANCE COMPANY;
PENNSYLVANIA INSURANCE GUARANTY ASSOCIATION;
UNITED STATES OF AMERICA;
UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
(D.C. Civil No. 88-02126)

THE FIDELITY & CASUALTY CO. OF NEW YORK

v.

THE TEXAS EASTERN TRANSMISSION CORP.
(D.C. Civil No. 88-05039)

TEXAS EASTERN TRANSMISSION CORPORATION

v.

FIDELITY & CASUALTY COMPANY OF NEW YORK;
ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD;
AETNA CASUALTY AND SURETY COMPANY;
AMERICAN HOME ASSURANCE COMPANY, a/k/a
AMERICAN HOME INSURANCE COMPANY;
BOSTON OLD COLONY INSURANCE COMPANY;
CIGNA INSURANCE COMPANY;
CONTINENTAL CASUALTY COMPANY;
EMPLOYERS MUTUAL CASUALTY COMPANY;
FIRST STATE INSURANCE COMPANY;
HIGHLANDS INSURANCE COMPANY;
THE HOME INSURANCE COMPANY;
THE INSURANCE COMPANY OF NORTH AMERICA;
INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA;
INTERNATIONAL INSURANCE COMPANY;
LEXINGTON INSURANCE COMPANY;
MIDLAND INSURANCE COMPANY
NATIONAL SURETY CORPORATION;
PRUDENTIAL REINSURANCE COMPANY;
RANGER INSURANCE COMPANY;
REPUBLIC INSURANCE COMPANY;
STONEWALL INSURANCE COMPANY;
UNITED STATES FIRE INSURANCE COMPANY;
CERTAIN UNDERWRITERS AT LLOYD'S, LONDON
and CERTAIN LONDON MARKET INSURANCE COMPANIES
(D.C. Civil No. 88-05707)

Texas Eastern Transmission Corporation,

Appellant

Appeal from the United States District Court
for the Eastern District of Pennsylvania

Present: MANSMANN, ALITO and ALDISERT, *Circuit Judges*.

ORDER

It is ORDERED that the Clerk of this court vacate the panel's opinion and judgment filed May 28, 1993, which vacatur was inadvertently omitted from our order dated August 18, 1993, granting panel rehearing.

BY THE COURT,

Circuit Judge

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 92-1638

IN RE: TEXAS EASTERN TRANSMISSION CORP. PCB CONTAMINATION INSURANCE COVERAGE LITIGATION
(MDL No. 764)

ASSOCIATED ELECTRIC & GAS INSURANCE SERVICES, LTD.; NATIONAL SURETY CORPORATION

vs.

TEXAS EASTERN TRANSMISSION CORPORATION; FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK; CERTAIN UNDERWRITERS AT LLOYDS OF LONDON, INCLUDING THE INSURANCE COMPANY OF IRELAND; AETNA CASUALTY AND SURETY COMPANY; AMERICAN HOME ASSURANCE COMPANY; BOSTON OLD COLONY INSURANCE COMPANY; CONTINENTAL CASUALTY INSURANCE COMPANY; FIRST STATE INSURANCE COMPANY; HIGHLANDS INSURANCE COMPANY; THE HOME INSURANCE COMPANY; INSURANCE COMPANY OF NORTH AMERICA; INSURANCE COMPANY OF THE STATE OF PENNSYLVANIA; INTERNATIONAL INSURANCE COMPANY; LEXINGTON INSURANCE COMPANY; MIDLAND INSURANCE COMPANY MUTUAL MARINE INSURANCE COMPANY; PRUDENTIAL REINSURANCE COMPANY; RANGER INSURANCE COMPANY; REPUBLIC INSURANCE COMPANY; STONEWALL INSURANCE COMPANY; PENNSYLVANIA INSURANCE GUARANTY ASSOCIATION; UNITED STATES OF AMERICA; UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
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STONEWALL INSURANCE COMPANY;
UNITED STATES FIRE INSURANCE COMPANY;
CERTAIN UNDERWRITERS AT LLOYD'S, LONDON
and CERTAIN LONDON MARKET INSURANCE COMPANIES
(D.C. Civil No. 88-05707)

Texas Eastern Transmission Corporation,

Appellant

Present: MANSMANN, ALITO AND ALDISERT,
Circuit Judges.

ORDER

The mandate in all three consolidated District Court cases in this appeal is stayed. The Petition for Panel Rehearing filed by appellees is hereby granted but is limited exclusively to the matters raised in the petition. Oral argument will be held on Thursday, September 30, 1993, at 2:00 p.m. The parties may file letter briefs in addition to their previously filed briefs. An original shall be filed with the Clerk's Office with a copy to each judge at his or her chambers. The appellant's brief will be due September 8, 1993, and the appellees' brief will be due on September 22, 1993. These briefs should address the following questions:

1) the structure and purpose of 28 U.S.C. § 1330;

2) what claims, if any, have been asserted by AEGIS against ICI;

3) whether the presence of all parties destroys supplemental jurisdiction in the F & C case.

In addition, the parties may present any further information they deem relevant. Appellant shall furnish the court with copies of the AEGIS complaint.

BY THE COURT,

_____

Circuit Judge

Dated: August 18, 1993

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 92-1638

IN RE: TEXAS EASTERN TRANSMISSION CORP. PCB CONTAMINATION INSURANCE COVERAGE LITIGATION (MDL No. 764)

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UNITED STATES FIRE INSURANCE COMPANY;
CERTAIN UNDERWRITERS AT LLOYD'S, LONDON
and CERTAIN LONDON MARKET INSURANCE COMPANIES
(D.C. Civil No. 88-05707)

Texas Eastern Transmission Corporation,

Appellant

Appeal from the United States District Court
for the Eastern District of Pennsylvania
District Judge: Honorable Donald W. VanArtsdalen

Argued
April 7, 1993
Before: MANSMANN, ALITO and ALDISERT, *Circuit Judges*.

(Filed MAY 28 1993)

OPINION OF THE COURT

MANSMANN, *Circuit Judge*.

Texas Eastern Transmission Corporation claimed that its comprehensive general liability insurance carriers (the "Carriers") must pay for damages associated with the cost of removing PCBs that present a danger of polluting the property of third parties. The district court granted summary judgment against Texas Eastern on the theory that Texas Eastern provided prejudicially late notice of its claim to the carriers. We will affirm.

I.

The relevant facts, which appear in great detail in the district courts opinion, may be summarized as follows.

Until the early 1970s, Texas Eastern Used a toxic, PCB-laden lubricant in compressor stations along a pipeline

that stretched 9,500 miles, from Texas to New York. The lubricant comingled with other toxic fluids in the pipeline, and Texas Eastern discharged those fluids into the environment, either by venting then into the air during start-up or shut-down, or by discharging them into earthen pits, which occasionally overflowed. Texas Eastern would also occasionally spray fluids from the pits to kill weeks or to control dust.

As early as 1972, the lubricant's manufacturer informed Texas Eastern that the lubricant contained toxic PCBS. Throughout the late 1970s and early 1980s, Texas Eastern became increasingly aware that PCBs were entering the environment via the pipeline fluid. The district court determined that, taking all inferences in favor of Texas Eastern, a genuine issue of material fact existed as to whether Texas Eastern knew between 1970 and December 1986 that PCBs were present in the pipeline fluid and that the PCBS could migrate, via the pipeline fluid, onto the property of third parties. That issue was critical because such knowledge would trigger Texas Eastern's obligation to notify Carriers of an insurable "occurrence" under the relevant insurance policies.

Employing the correct summary judgment standard, the district court determined that although a rational factfinder could conclude that Texas Eastern knew PCBs were migrating to the property of third parties as early as 1972, December of 1986 was the latest possible date a jury could conclude that Texas Eastern discovered that PCBs were migrating onto the property of third parties. The district court based its determination in part on Texas Eastern's concession that in December, 1986, a preliminary report commissioned by Texas Eastern gave it reason to know that PCBs were migrating off-site.

As we review in more detail below, between December, 1986, and August, 1987, Texas Eastern entered into at least one consent decree and negotiated in earnest with the Environmental Protection Agency. After some months of negotiation with EPA, Texas Eastern notified the Carriers of a potential occurrence giving rise to a claim. The cost of clean-up is now estimated at $750 million.

Fidelity and Casualty, Texas Eastern's primary carrier, brought a suit premised on diversity jurisdiction, seeking a declaratory judgment that it was not liable under its policy for the claims. Associated Electric & Gas Insurance Services, Ltd. ("AEGIS") and National Surety Corporation, other carriers of Texas Eastern, brought a second suit against Texas Eastern and all of the remaining carriers. Federal subject matter jurisdiction in the *AEGIS* action was premised on the Foreign Sovereign Immunities Act, which we will address below. Texas Eastern brought a third, state-court action against all the carriers. That action was removed to federal court, also on the basis of the Immunities Act.

In an extensive opinion, the district court determined that summary judgment should be entered against Texas Eastern on the ground that its delay in providing notice to the Carriers was unreasonable and prejudicial as a matter of law. *In re Texas Eastern Transmission Corporation PCB Contamination Insurance Coverage Litigation*, No. MDL-764 (E.D. Pa. July 9, 1992).

We exercise plenary review of the district court's grant of summary judgment, applying "the same test the district court should have used initially." *Goodman v. Mead Johnson & Co.*, 534 F.2d 566, 573 (3d Cir. 1976), *cert. denied*, 429 U.S. 1038 (1977). *See generally Celotex Corp. v. Cartrett*, 477 U.S. 317 (1986); *Anderson v. Liberty*

Lobby, Inc., 477 U.S. 242 (1986); *Matsushita Electric Industrial Co. v. Zenith Radio Corp.*, 475 U.S. 574 (1986).

II.

As a threshold matter, we have established that the district court had subject matter jurisdiction over the dispute. Of the three cases that constitute this multi-district litigation, one is properly premised on diversity jurisdiction under 28 U.S.C. § 1332. *Fidelity & Cas. Co. v. Texas Eastern,* No. 88-05039. The other two cases, *Associated Electric & Gas Ms. Svs. v. Texas Eastern,* No. 88-021267 ("*AEGIS*") and *Texas Eastern v. Fidelity & Cas. Co.*, No. 88-05707, are premised on jurisdiction under the Foreign Sovereign Immunities Act, which provides: "The district courts shall have original jurisdiction without regard to amount in controversy of any nonjury civil action *against* a foreign state . . . . " 28 U.S.C. § 1330(a) (emphasis added). In each of these two cases, Immunities Act jurisdiction results from the presence as a defendant of the Insurance Corporation of Ireland, Ltd. ("ICI"), which qualifies as a "foreign state" because the Republic of Ireland owns 100% of its stock and has assumed its obligations. *See* 28 U.S.C. § 1603 (definition of "foreign state").

Texas Eastern has suggested that in the *AEGIS* case, we must realign ICI as a plaintiff because ICI (a carrier) shares the common purpose with AEGIS (another carrier) of avoiding liability to Texas Eastern. *Cf. Employers Ins. of Wausau v. Crown Cork & Seal Co.*, 942 F.2d 862 (3d Cir. 1991) (realigning all insurers against insured to defeat *diversity* jurisdiction). Texas Eastern, proceeding on the false premise that realignment applies to Immunities Act cases, argues that once the court realigns ICI as a plaintiff, the suit is no longer "against" a foreign state and therefore no longer subject to federal jurisdiction under 28 U.S.C. § 1330(a).

Realignment, a creature of diversity jurisprudence, serves the purpose of insuring the existence of complete diversity. *See generally* Wright, Miller & Cooper, Federal Practice & Procedure: Jurisdiction 2d § 3607, and cases cited therein. Complete diversity, however, is a concept foreign to the Immunities Act. Therefore, application of realignment to Immunities Act jurisdiction would not serve any purpose.

Indeed, Texas Eastern has not provided any authority to support the novel application of realignment to Immunities Act cases, nor are we aware of any binding authority. *But see Liberty Mutual Ins. v. Insurance Corp. of Ireland,* 693 F. Supp. 340 (W.D. Pa. 1988) (Mencer, J.) (presuming realignment would apply to Immunities Act cases).

Moreover, assuming arguendo that realignment did apply, Texas Eastern fails to explain why ICI should be realigned as a plaintiff. In *Texas Eastern v. Fidelity and Casualty, et al*, removed to the federal court on the basis of the Immunities Act, Texas Eastern sued all of its carriers *as defendants*. Texas Eastern has not articulated a principled reason to realign ICI as a plaintiff in the *Texas Eastern* case, nor are we aware of any.[1/] Thus, even if realignment could apply to defeat subject matter jurisdiction in the *AEGIS* case, realignment would not defeat subject matter jurisdiction in the *Texas Eastern* case, and the parties

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[1/] Even if, under some version of the well-pleaded complaint rule, we could not construe the *AEGIS* complaint to state any cause of action against ICI, we would be compelled under the same rule to construe Texas Eastern's complaint as stating a claim against ICI. Moreover, we note that the "well-pleaded complaint" rule does not necessarily apply to Immunities Act cases. *See Verlinden B. V. v. Central Bank of Nigeria,* 461 U.S. 480, 494-95 (1983).

and the dispute would be properly before the federal court.[2/]

We have jurisdiction of a final decision of the district court. 28 U.S.C. § 1291.

III.

In determining that late notice relieved the Carriers of any obligation under the contracts, the district court reached three central conclusions. First, Texas Eastern's duty to inform the carriers of an "occurrence" accrued not later

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2/ Texas Eastern suggests that ICI's contractual consent to appear in "any court of competent jurisdiction" deprives the federal courts of jurisdiction under the Immunities Act. We do not, however, construe the contractual waiver as anything more than a waiver of the right to contest in personam jurisdiction. In *Foster v. Chesapeake Ins. Co., Ltd*, 933 F.2d 207 (3d Cir. 1991), we held that a similar contractual provision constituted a waiver of the right to remove a *diversity suit*. We expressly recognized, however, that the Court of Appeals for the Sixth Circuit, "primarily driven by considerations peculiar to the FSIA," reached the opposite result with respect to removal of a suit premised on Immunities Act jurisdiction. *Id.* at 1218 n.15. While the dissent does not find the Diversity/Immunities Act distinction significant, dissent at 3, we have already acknowledged some "peculiar" distinctions. *Foster*, 933 F.2d at 1218 n.15

Moreover, Texas Eastern argued on appeal that because of the contractual waiver, "there was never federal jurisdiction over the TETCO action." Br. of Appellant at 69. In this argument, Texas Eastern was clearly incorrect. The waiver would not deprive a federal court of its competency, under Article III and under the laws of the United States, to pass on the merits of the dispute. While parties may agree not to litigate in federal court, they cannot, by contract, destroy a federal court's subject matter jurisdiction any more than they can confer it by contract.

than December of 1986. Second, Texas Eastern provided unreasonably late notice to the Carriers eight or nine months later, in August of 1987. Third, the unreasonably late notice prejudiced the Carriers. Although Texas Eastern challenges all three conclusions, only the third, regarding prejudice, merits some discussion.

A.

To predict the standard of prejudice applied under Texas law, we must first review the relevant line of Texas cases. The Texas Supreme Court long adhered to the rule that an insured's delay in providing notice relieved a carrier of liability under the policy, even in the harsh case when the carrier stipulated that it had not suffered any prejudice at all. *See Members Mutual Ins. Co. v. Cutaia,* 476 S.W.2d 278 (Tex. 1972) (stating harsh rule).

In 1973, the Texas State Board of Insurance ordered that the following Amendatory Endorsement be attached to general liability policies:

> As respects *bodily injury* liability coverage and *property damage* liability coverage, unless the company is prejudiced by the insured's failure to comply with the requirement, any provision of this policy requiring the *insured* to give notice of action, *occurrence* or loss, or requiring the *insured* to forward demands, notices, summons or other legal process, shall not bar liability under this policy.

See R. at 869-72 (Order of Insurance Board).

Our task is to determine what constitutes prejudice, under Texas law, as a matter of law. Although "there is a paucity of authority explicating what, within the purview of the endorsement, would constitute prejudice sufficient to relieve an insurer of liability," *Kimble v. Aetna Casualty & Surety Co.*, 767 S.W.2d 846, 850 (Tex. App. Ct. 1989), at least one Texas appellate court has stated clearly that prejudice results to the insurer by "*the change in its position*" brought about by an insured's failure to notify. *Members Ins. Co. v. Branscum*, 803 S.W.2d 462, 466 (Tex. Ct. App. 1991) (emphasis added) (citing *Kimble*, 767 S.W.2d at 851).

While we find helpful the change-in-position elaboration on the legal meaning of prejudice, the question remains how substantial that change in position must be before a court can conclude that, as a matter of law, a carrier has suffered prejudice. In some states, for example, courts have imposed a "substantial prejudice" standard, which requires a demonstration that an insurer *could* have either defeated a claim or settled for a smaller sum than the sum for which the insured ultimately settled. *Insurance Co. of Pa. v. Associated Int'l Ins. Co.*, 922 F.2d 516, 524 (9th Cir. 1990) (applying California law). To determine the extent of harm sufficient to constitute prejudice under Texas law, we find instructive the facts of several Texas cases.

In a number of cases, Texas courts have held that notice to a carrier after the entry of a default judgment has become final constitutes prejudice, as a matter of law, sufficient to defeat the carrier's liability under a policy. *See, e.g., Ratcliff v. National County Mut. Fire Ins. Co.*, 735 S.W.2d 955, 957 (Tex. Ct. App. 1987). *Compare Allstate Ins. Co. v. Pare*, 688 S.W.2d 680 (Tex. Ct. App. 1984) (no prejudice where insurer received papers before default and had negotiated for settlement prior to default).

Notably, the court in *Ratcliff* did not require the carrier to show that it would have or could have defended the suit successfully or reached a better settlement. We note also that in the *Kimble* court determined that prejudice existed notwithstanding that the carrier learned of the suit before the judgment became final. 767 S.W.2d at 850. Observing that opening of the judgment was uncertain, the court did not assign any burden to the carrier to show that it would have litigated the case or to explain why it did not alter the litigation. *Id.* at 850-51. Similarly, in *Branscum,* the court held that prejudice resulted when a carrier learned of a final default judgment, notwithstanding that the carrier had had actual knowledge of the underlying accident, had engaged in settlement negotiations, and had known of an impending suit. 803 S.W.2d at 463-64.

These cases demonstrate that the Texas courts do not utilize a "substantial prejudice" standard and do not impose on carriers the burden of explaining non-action such as failure to obtain papers in an impending suit. Indeed, the court in *Branscum* stated unequivocally that "application of a 'substantial' prejudice standard is erroneous." *Branscum*, 803 S.W.2d at 467.

Upon review of the Texas caselaw discussed above, we predict that the Texas courts would apply a standard of prejudice defined in terms of a change in position adverse to a carrier's interest. *See Branscum,* 803 S.W.2d at 466; *Kimble,* 767 S.W.2d at 851. Although the change must obviously be material under this standard of prejudice, the carrier need not show that the change is irreversible in order to demonstrate that prejudice has resulted. *E.g.*, *Kimble,* 767 S.W.2d at 851 (holding of prejudice, notwithstanding carrier's rejection of option to petition to vacate default). With these decisions in mind, we turn now to a review of the district court's conclusion.

B.

In concluding that the Carriers were prejudiced by Texas Eastern's delay of at least eight months in providing notice, the district court assumed without deciding that prejudice was a necessary element to the Carrier's defense of late notice. The district court then examined the events that the parties do not dispute took place between December, 1986 (the latest date that the duty to notify accrued), and late August, 1987 (the date Texas Eastern actually gave notice to the Carriers).

On December 15, 1986, several days after it had received from its broker a comprehensive list of carriers and notice provisions, Texas Eastern proposed a cleanup plan to the EPA. Op. at 149. (Four days later, Texas Eastern met with EPA officials to discuss the establishment of a framework for future discussions on remediating contaminated on-site areas on Texas Eastern's system. R. at 1036-37. Within a month, Texas Eastern had furnished EPA with a summary of a preliminary environmental report and a "Summary of Dioxin Sampling and Analysis." R. at 1036, ¶ 375-76.)[3/] As the district court noted:

> By this time, Texas Eastern was committed to remediating the PCB contamination in its unlined earthen pits and the only material dispute between Texas Eastern and EPA was the extent of

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[3/] Here and in the following paragraphs, we have noted parenthetically specifics to which the district court did not refer expressly.

> the cleanup and the form of the agreement which would be required.

Op. at 149.

In February of 1987, at approximately the same time that the Houston Chronicle published an article detailing Texas Eastern's PCB-related problems, Texas Eastern considered giving notice, but did not. Op. at 150-51. On March 17, Texas Eastern testified before a United States Senate Subcommittee regarding its PCB problem and the status of its *already* ongoing settlement discussions with EPA. And in April, settlement negotiations became intensive, with EPA insisting that cleanup levels be based on EPA's "risk assessments" and with EPA demanding that Texas Eastern consider off-site contamination and enter into formal negotiations to discuss specific cleanup demands. Op. at 151-52. It was at this point that Texas Eastern entered into a consent decree with the Commonwealth of Pennsylvania. Op. at 172. (That decree contained numerous stipulations of fact, and it established testing and monitoring methodologies and schedules that Texas Eastern would follow. R. at 4968.)

By mid-August, significant and extensive negotiations had already taken place, as indicated by the contents of a letter dated August 18 from Carol Dinkins, Texas Eastern's negotiator, to EPA. Op. at 152. The letter summarizes fifteen major issues for inclusion in a comprehensive settlement, among then Texas Eastern's proposal to pay substantial civil penalties and oversight costs. R. at 808-809. (The letter also discloses Texas Eastern's bargaining position: "Texas Eastern proposes to undertake a far greater commitment of work at many more sites than EPA has ever seen any party voluntarily stop forward to work out . . . ." R. at 809.) A few days later, Texas

Eastern mailed its notice of claim, dated August 19, 1987, to the Carriers.

> With respect to these events, the district court held:
>
> By the time Texas Eastern gave notice, remedial efforts, testing and monitoring had begun, and schedules and methodologies to characterize the sites had been established. Most importantly, Texas Eastern had already presented to EPA its proposed settlement terms, and thus completely destroyed any meaningful opportunity for the Carriers to shape negotiations with EPA. The record makes it abundantly clear that Texas Eastern never wanted the Carriers to interfere with what was a carefully negotiated settlement with EPA and waited until the settlement was substantially agreed upon before providing any notice to the Carriers.

Op. at 172-73.

Texas Eastern does not dispute that, by August 19, 1987, the Carriers had lost an opportunity to participate initially in "remedial efforts, testing, . . . monitoring, and [establishment of] schedules and methodologies." Op. at 172-73. Indeed, Texas Eastern's assertion that insurers do not generally get involved in environmental investigations and negotiations is without record support. *See* Br. for Appellant at 31; Rep. Br. for Appellant at 3 n.3. Nor does Texas Eastern dispute that, as of August 18, 1987, at least one day before notice was provided, Texas Eastern had *already* disclosed its bargaining position to EPA, or, in the

parlance of poker players, tipped its hand by, for example, proposing to pay a substantial civil penalty and to undertake a voluntary cleanup far greater than EPA had ever seen. Under the law of Texas, these undisputed facts alone justify the district court's holding because they indicate prejudice resulting from a material change in the Carriers' bargaining position. *See Branscum,* 803 S.W.2d at 466. Because the above changes resulted in prejudice, we need not address the Carriers' additional arguments that prejudice resulted from Texas Eastern's waiver of rights against the United States and from Texas Eastern's renewal of its insurance contracts prior to notifying the Carriers of the claim.

C.

Because prejudice flows from the bargaining position as developed by Texas Eastern through its field investigations and in its negotiations, it follows that Texas Eastern's disputations that "there was no 'done deal' between Texas Eastern and EPA in August, 1987" are of no weight. The district court remarked not that the matter was a "done deal," but that "the matter was for *all intents and purposes* . . . a 'done deal.'" Op. at 170 (emphasis added). Indeed, most, if not all, of the points in the August 18 letter found their way, in some form or other, into the final consent decree. *Compare* R. at 805 (Dinkins's letter) *with* R. at 557 (consent decree).

Moreover, Texas Eastern's assertions that the Carriers had the option of entering the negotiations after August 18, 1987, are immaterial to the issue of whether prejudice occurred *prior* to that date through a material change in position. In *Kimble,* a carrier chose not to enter litigation, even though there remained time to do so. 767 S.W.2d at 846. As the court in *Branscum* noted:

> The *Kimble* court held that prejudice results to the insurer by the change in its position brought about by the insured's failure to forward the suit papers until after the default. Prejudice results *even though the option to file a new trial is still available to the insurer. Kimble,* 767 S.W.2d at 851.

Branscum, 803 S.W.2d at 466 (emphasis added). By analogy, prejudice resulted here even though the option to enter negotiations was still available to the Carriers.

Texas Eastern submits one further challenge to the district court's determination of prejudice, namely, that the Carriers must show that they would have entered negotiations earlier and that they could have altered the outcome. This challenge, however, seeks to apply the "substantial prejudice" standard to the Carriers, whereas the tone and tenor of extant Texas caselaw indicates that the application of that standard would be erroneous.[4/] *See, e.g., Branscum,* 803 S.W.2d at 467.

[4/] The position of the dissent, that the carriers must demonstrate that they *would* have entered into negotiations in order to demonstrate prejudice from late notice, *see* dissent at 11, does not comport with our reading of the Texas caselaw. Moreover, the dissent's approach would inappropriately render a notice defense unavailable under Texas law any time a carrier also asserted other bona fide defenses to coverage.

For example, a carrier might refuse to defend against a battery claim on the grounds that a policy clearly limited the carrier's obligation to the defense of negligence. That carrier would never be able to meet the dissent's "actual prejudice" standard, no matter how egregious the lateness of notice.

D.

Because we have determined that the district court correctly concluded that the carriers were prejudiced, we need not address the remaining contentions of Texas Eastern.

IV.

For the foregoing reasons, we will affirm the judgment of the district court.

TO THE CLERK:

Please file the foregoing opinion.

Ciruit Judge

In Re: Texas Eastern Transmission, No. 92-1638

ALITO, *Circuit Judge,* concurring in part and dissenting in part.

I disagree with the majority's conclusion that the district court properly reached the substantive merits of all three of the cases before it. I conclude instead that the district court erred in ruling on the merits of two of the three cases. I also disagree with the majority's holding that summary judgment was properly granted against Texas Eastern Transmission Corporation ("TETCO") on the question of whether the lateness of its notification to its insurers caused any actual prejudice. I therefore dissent in part.

I.

Three different civil actions were consolidated for decision in the district court by the Judicial Panel on Multidistrict Litigation. No challenge is made to the propriety of the district court's deciding the merits of one of those actions, *i.e.*, the case originally brought by Fidelity & Casualty Company of New York ("F & C") against TETCO in the United States District Court for the Northern District of Texas. The merits of the other two cases, however, were not properly in federal court.

A. One of these cases, Eastern District of Pennsylvania docket number 88-05707, was originally filed by TETCO in state court in Texas, naming all of TETCO's many excess liability carriers as defendants. It was then removed to federal court by one of the defendants, the Insurance corporation of Ireland (ICI), pursuant to 28 U.S.C. § 1441(d), which permits removal of a civil action "against a foreign state as defined in [28 U.S.C.] section

1603(a)." Assuming for the sake of argument that ICI falls within the § 1603 definition of a "foreign state," this removal appears at first glance to have been proper.[1/] However, the insurance contract between TETCO] and ICI contained the following clause:

> It is agreed that in the event of the failure of the Underwriters hereon [i.e., ICI] to pay any amount claimed to be due hereunder, Underwriters hereon at the request of the Insured (or Reinsured) [i.e., TETCO) will submit to the jurisdiction of any court of competent jurisdiction within the United States and will comply with all requirements necessary to give such Court jurisdiction and all matters arising hereunder shall be determined in accordance with the law and practice of such Court.

TETCO timely moved in the district court for this action to be remanded to Texas state court on the theory that this clause was an enforceable contractual waiver of ICI's statutory right to remove lawsuits against it to federal court.[2/] The district court denied this motion. Subsequent to the district court's ruling on this issue, we decided *Foster*

[1/] The district court held that ICI was a "foreign state" as defined in 28 U.S.C. § 1603(a). TETCO argued to the contrary in the district court and renews that argument on appeal. The district court's holding seems correct, but I do not find it necessary for me to reach that question.

[2/] Because there is no other statutory ground for this action to be in federal court, a remand would have been required if ICI's removal was not proper.

v. Chesapeake Insurance Co., Ltd., 933 F.2d 1207 (3d Cir. 1991), which concerned a reinsurance agreement containing a virtually identical clause. We interpreted the clause to constitute a waiver of the statutory right to remove based on diversity of citizenship and held that the clause was not unenforceable as unreasonable or against public policy. *Accord City of Rose City v. Nutmeg Insurance Co.*, 931 F.2d 13, 14-16 (5th Cir. 1991). *But see In re Delta America Re Insurance Co.*, 900 F.2d 890 (6th Cir. 1990) (similarly worded clause did not waive removal under 28 U.S.C. § 1441(d)); *Proyecfin de Venezuela, S.A. v. Banco Industrial de Venezuela, S.A.*, 760 F.2d 390 (2d Cir. 1985) (differently worded clause did not waive removal under § 1441(d)). While our decision in *Foster* concerned removal under 28 U.S.C. § 1441(a) rather than § 1441(d), I do not find this distinction significant for present purposes. Accordingly, I would apply *Foster* to this case and hold that ICI waived its statutory right to remove the TETCO action to federal court and that it was therefore reversible error for the district court to deny TETCO's motion requesting a remand to state court. I would consequently vacate the district court's grant of summary judgment to the insurers in this action and remand the case to the district court with instructions to remand to the Texas state court.

B. Another of the actions that was before the district court, docket number 88-02126, was originally filed in the United States District Court for the Eastern District of Pennsylvania by two of TETCO's excess liability insurers, Associated Electric & Gas Insurance services (AEGIS) and National Surety (NS), naming as defendants TETCO, F & C, and all of TETCO's other excess liability insurers, one

of which was ICI.[2/] The only suggested basis for the subject matter jurisdiction of the federal court over the action is 28 U.S.C. § 1330(a), which confers jurisdiction over certain civil actions "against a foreign state as defined in [28 U.S.C.] section 1603(a)." (I again assume arguendo that the district court's conclusion that ICI is a "foreign state" is correct.) It is clear from the complaint that the primary objective of this action was to obtain a declaratory judgment that TETCO was not entitled to coverage under any of the policies issued to it by the two named plaintiffs. In the alternative, the plaintiffs sought a declaratory judgment regarding the rights and obligations of the various insurers with respect to each other.

I do not believe that a civil action can be regarded as "against" a foreign state for purposes of § 1330(a) jurisdiction unless the legal interests of the named plaintiff or plaintiffs, on the one hand, and the legal interests of the foreign state, on the other hand, are sufficiently adverse that the action would be considered "between" parties of diverse citizenship for purposes of basing jurisdiction on 28 U.S.C. § 1332(a). Identifying such an actual adversity of interest, rather than simply accepting the nominal alignment of parties declared on the face of the pleadings, is especially important because § 1330 bestows jurisdiction on actions involving foreign state defendants under a wider array of circumstances than other statutory provisions bestow jurisdiction on actions involving foreign state plaintiffs. In *Employers Insurance of Wausau v. Crown Cork & Seal Co., Inc.*, 905 F.2d 42, 46 (3d Cir. 1990), we held that unless there is a "real dispute on a primary issue in the controversy" between A and B, the case is not "between" A

2/ The original complaint in this action also named as defendants various governmental entities, all of which were subsequently dropped.

and B for purposes of the diversity jurisdiction statute. That test cannot be satisfied in the current case.[4] There is no "real dispute on a primary issue in the controversy" between either AEGIS or NS on the one hand and ICI on the other.

Employers Insurance of Wausau and related cases teach that when the nominal alignment of the parties on the pleadings does not reflect the underlying reality of adversity of interest, the court must "realign" the parties according to their true interests and see whether any basis for the jurisdiction of the federal courts remains. Two obvious realignments are possible here. The insurers contend that "the logical alignment is TETCO as plaintiff and the Carriers [including AEGIS and NS] as defendants" (Appellees' Joint Brief at 66). While this alignment would make the action "against" ICI, I do not find it plausible. Its most obvious flaw is that it would involuntarily render TETCO the plaintiff while denying TETCO the important plaintiff's prerogative of choosing the forum for the litigation. Indeed, such an alignment would make the case almost exactly identical to the action TETCO originally filed in its preferred forum. In addition, by making the primary defendant, TETCO, into the plaintiff and the original plaintiffs into defendants, such an approach could easily justify subverting the limitations of § 1330 by turning any action with a foreign state party into an action "against" the foreign state.

The other possible alignment of parties is all of the insurers, including ICI, as plaintiffs against TETCO as sole defendant. Jurisdiction exists, given an amount in

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[4] Like *Foster*, this case was decided after the district court ruled on the relevant issue.

controversy in excess of $50,000, for civil actions "between . . . a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States." 28 U.S.C. § 1332(a)(4). At least one court has held that this section does not confer jurisdiction on an action where there are any plaintiffs other than the foreign state or states. *L'Europeenne de Banque v. Republic of Venezuela,* 700 F. Supp. 114, 126 (S.D.N.Y. 1988). Even if § 1332(a)(4) can support jurisdiction where the foreign state plaintiff has co-plaintiffs which are not foreign states, I believe in the absence of clear Congressional intent to the contrary that "[t]he rule of complete diversity — that no plaintiff and no defendant may be a citizen of the same state — applies." *F. & H.R. Farman-Farmian Consulting Engineers Firm v. Harza Engineering Co.,* 882 F.2d 281, 284 (7th Cir. 1989). For cases brought under what is now § 1332(a)(1) this rule has been established since *Strawbridge v. Curtiss,* 7 U.S. 267 (1806). It also applies to cases brought under § 1332(a)(2). *Newman-Green, Inc. v. Alfonzo-Larrain,* 490 U.S. 826 (1989); *Depex Reina 9 Partnership v. Texas Int'l Petroleum Corp.,* 897 F.2d 461 (10th Cir. 1990); *Farman-Farmian, supra.* There have been a few cases brought under § 1332(a)(3) where jurisdiction has been held not to be destroyed by the presence of aliens on both sides of the litigation — even aliens who are citizens of, or corporations incorporated in, the same foreign country — but in all of these cases the American plaintiffs have been completely diverse as to state citizenship from the American defendants. *E.g., Clark v. Yellow Freight System, Inc.,* 715 F. Supp. 1377 (E.D. Mich. 1989); *K & H Business Consultants, Ltd. v. Cheltonian, Ltd.,* 567 F. Supp. 420 (D.N.J. 1983) (detailed analysis of problem per Debevoise, J.); *Samincorp, Inc. v. Southwire Co., Inc.,* 531 F. Supp. 1 (N.D. Ga. 1980). TETCO is treated by the diversity jurisdiction statute as if it were a citizen both of Delaware, where it is incorporated,

and Texas, where it maintains its principal place of business. 28 U.S.C. § 1332(c)(1). Quite a number of TETCO's insurers other than ICI are either incorporated or maintain their principal p[illegible]ce of business in either Delaware or Texas. Therefore, I conclude that jurisdiction is not available under § 1332(a)(4). For these reasons, I would hold that the district court did not have jurisdiction over the subject matter of this action, and would therefore vacate the grant of summary judgement to the insurers against TETCO and remand with instructions to dismiss the action for lack of jurisdiction.

II.

I now turn to the merits of the remaining case that was before the district court, the declaratory judgment action originally brought by against TETCO by F & C., TETCO's primary CGL insurer. This action involved the availability of coverage for TETCO's PCB-related problems under a series of policies that were in effect from 1961 through 1988. All of these policies generally required TETCO to notify F & C "as soon as practicable" after becoming aware of an "occurrence" that appeared likely to trigger coverage. For the policies effective on or after May 1, 1973, in order to deny coverage the insurer must show that it has suffered some degree of actual prejudice from the insured's failure to give notice as soon as practicable. For the earlier policies, lack of timely notice is sufficient to deny coverage without any inquiry into prejudice caused or not caused thereby. The policies in effect from July 1, 1970 through January 1, 1981 also contained a clause excluding coverage for damage caused by pollution unless the pollution was "sudden and

accidental.[5/] The earlier and later policies do not contain this exclusion.

Since TETCO's policies with F & C provided coverage for damage to the property of others but not to TETCO's own property, the notice requirement meant, as the district court concluded, that TETCO was obligated to notify its insurers promptly upon learning that PCBs were migrating beyond its own property lines, since off-site migration was the "occurrence" likely to produce claims potentially covered by the policies.[6/] The district court held that this notice obligation accrued no later than December 1986, when TETCO received a report documenting off-site PCB migration. But even if this obligation did not arise until as late as May 1987 — when the EPA demanded cleanup

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[5/] The clause reads:

> This policy does not apply . . . to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any watercourse or body of water; but this exclusion does not apply if such discharge, dispersal, release or escape is sudden and accidental.

[6/] Because of my conclusion that the merits of the coverage dispute between TETCO and its excess insurance carriers were not properly before the district court, I need only consider the effect of TETCO's late notice on F & C alone. However, since the majority considers the effect of late notice on all of the insurers, and I agree that the same analysis would apply to the excess insurers as to F & C, I also write in terms of the effect of the late notice on the insurers as a class, including both F & C and the excess insurers.

measures aimed at preventing additional off-site migration — TETCO's notice in August 1987 could not reasonably be regarded as having been given "as soon as practicable." TETCO is certainly capable of moving more quickly than that when its own interests are at stake. Thus, I agree with the district court and the panel majority that TETCO did not comply with its notice obligation. On this basis, I agree that the district court properly granted summary judgment to F & C declaring coverage unavailable as to the earliest sequence of policies — those without an actual prejudice requirement.

Under Texas law, however, late notice destroys coverage for more recent policies only if the insurer suffers actual prejudice (*see* Maj. Op. 9-12). Unlike the majority, I am convinced that summary judgment for the insurers on this issue was improper. The majority correctly observes that TETCO's late notice deprived the insurers of the opportunity to participate in the settlement negotiations between TETCO and the EPA that took place during the summer of 1987. I wholeheartedly agree that these were important discussions and that the insurers suffered prejudice *if, given the opportunity, the insurers would have participated at least seriously considered participation in these discussions*. But what if the insurers would not have participated or even seriously considered doing so? Could it then be said that they suffered prejudice in any meaningful sense? I do not think so.

Before holding that TETCO's claims are barred because the insurers were prejudiced, I think we should require at least some support in the summary judgment record indicating that the insurers would or realistically might have availed themselves of the supposedly valuable opportunity that they lost. There is, however, no such support—no affidavits or other support concerning (a) what the insurers

would have done in this case had they received prompt notice, (b) these insurers' general involvement in EPA settlement negotiations in cases such as this, or (c) prevailing practices in the insurance industry as a whole in comparable cases.

This is a case in which the insurers had huge potential liability, but also had many promising legal defenses. Under these circumstances, it may well be that the insurers, if given prompt notice, would have summarily concluded that the best strategy was to let TETCO negotiate on its own and then fight any subsequent TETCO claims. This is precisely the strategy that they did adopt after TETCO's notice was received. Without anything in the summary judgment record to show that the insurers would not have taken this approach had they received notice more promptly, I do not think that summary judgment on this issue was proper on the present record.

III.

While I cannot agree that the insurers were entitled to summary judgment on the issue of actual prejudice, I agree that the insurers were entitled to summary judgment with respect to some of the policies on an alternative ground cited by the district court, *i.e.*, the presence of a pollution exclusion clause in some but not all of the relevant policies.

The district court made an alternative holding that summary judgment would be proper against TETCO as to these policies because damage caused by the off-site PCB migration was pollution damage that was not "sudden and accidental." For essentially the reasons given by the district court at page 123 *et seq.*, of its opinion, I believe that this alternative holding was correct and that therefore the district court's grant of summary judgment in favor of F & C as to

the policies with an actual prejudice requirement that contain the pollution exclusion should be affirmed on this alternative ground.[7/]

IV.

In sum, I would vacate the grant of summary judgment in the two cases involving TETCO's excess insurers and instruct the district court to remand the action originally filed by TETCO (its docket number 88-05707) to state court in Texas and to dismiss the action originally filed by AEGIS and NS (its docket number 88-02126). I would affirm in part and vacate in part the grant of summary judgment to F & C in the remaining case, and remand that case to the district court for further proceedings.

7/ After this case was argued, the intermediate appellate court in Texas issued an opinion construing the "sudden and accidental" language that TETCO argues supports its position that coverage is available. *Circle "C" Ranch Co. v. St. Paul Fire & Marine Insurance Co.*, No. 3-91-388-CV, 1993 WL 142131 (Tex. Ct. App. May 5, 1993). I agree that this opinion provides some additional support to TETCO's contention that the off-site PCB migration was "accidental" under Texas law regardless of the fact that the discharge of the PCBs into the unlined on-site pits was intentional. However, for the pollution exclusion not to bar coverage, the off-site PCB migration would have to have been both sudden *and* accidental. The incident in *Circle "C"* — aerial spraying on the insured's land of chemicals which drifted onto the insured's neighbor's cotton — was "sudden." The opinion concerned only whether the unforeseen drift of the intentionally sprayed chemical was "accidental." I remain convinced that the district court correctly concluded that the PCB migration here cannot be considered even arguably "sudden."

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

	)	MDL DOCKET
In re	)	NO. 764
TEXAS EASTERN	)	ALL CASES
TRANSMISSION CORPORATION	)	
PCB CONTAMINATION	)	(No. 88-2126)
INSURANCE	)	(No. 88-5039)
COVERAGE LITIGATION	)	(No. 88-5707)
	)	

NOTICE OF APPEAL

Notice is hereby given that Texas Eastern Transmission Corporation, plaintiff in No. 88-5707 and defendant in Nos. 88-2126 and 88-5039, hereby appeals to the United States Court of Appeals for the Third Circuit from the final judgment entered in these consolidated cases on July 10, 1992; from the opinion and order entered July 10, 1992, denying Texas Eastern's motion for leave to amend its pleadings; and from the opinion and order of September 15, 1988, denying Texas Eastern's motions to

dismiss or stay Nos. 88-2126 and 88-5039 and to remand No. 88-5707 to the District Court of Harris County, Texas, 215th Judicial District.

Dated: August 6, 1992

Peter J. Nickles
Coleman S. Hicks
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IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In re	: MDL DOCKET NO. 764
TEXAS EASTERN TRANSMISSION	: ALL CASES
CORPORATION PCB CONTAMINATION	:
COVERAGE INSURANCE LITIGATION	:

OPINION

VanARTSDALEN, S.J. July 9, 1992

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I. INTRODUCTION

Texas Eastern Transmission Corporation (Texas Eastern), the owner-operator of a natural gas pipeline system extending from natural gas well fields in Texas, Louisiana, and the Gulf of Mexico to the New York metropolitan area, brought suit against approximately twenty-one insurance companies[1/] (the Carriers) that provided Texas Eastern with primary and excess comprehensive general liability (CGL) insurance coverage between 1958 and the present.[2/] Texas Eastern seeks to recover the expense that it will incur in the governmentally

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1/ The insurance companies include Fidelity & Casualty Company of New York, Associated Electric & Gas Insurance Services Limited, Aetna Casualty & Surety Company, American Home Assurance Company, Boston Old Colony Insurance Company, Continental Casualty Company, First State Insurance Company, Highlands Insurance Company, The Home Insurance Company, The Insurance Company of North America, Insurance Company of the State of Pennsylvania, Lexington Insurance Company, Midland Insurance Company (in receivership), National Surety Corporation, Prudential Reinsurance Company, Ranger Insurance Company, Republic Insurance Company, Stonewall Insurance Company, United States Fire Insurance Company, Certain Underwriters at Lloyd's, London, and Certain London Market Insurance Companies.

2/ Texas Eastern and the individual Carriers filed a Joint Submission of Texas Eastern Policies in which they stipulated to the existence of approximately fifty-seven insurance policies. Texas Eastern and the London Market Insurers filed a Stipulation in which they agreed to the existence of an additional fifty-three insurance policies.

mandated environmental cleanup of polychlorinated biphenyl[3/] (PCB) contamination at multiple locations on Texas Eastern's property along the transmission line. The total costs are estimated to exceed $750 million. After more than two years of discovery, the parties have now filed cross-motions for summary judgment.

II. PROCEDURAL HISTORY

The present litigation consolidates three lawsuits, each seeking declaratory judgment as to the respective duties and liabilities of the Carriers to defend and/or indemnify Texas Eastern against claims and settlements made by and with the United States Environmental Protection Agency (EPA), various state agencies, and private parties.[4/]

On December 11, 1987, Fidelity & Casualty Company of New York (Fidelity or F & C), Texas Eastern's primary CGL carrier throughout all relevant periods, filed Case No. 87-2925T against Texas Eastern in the United States District Court for the Northern District of Texas (Northern District action). The Northern District action was a diversity case establishing federal subject-matter jurisdiction pursuant to 28 U.S.C. § 1332.

[3/] A polychlorinated biphenyl is defined as "Any of a family of industrial compounds produced by chlorination of biphenyl, noted chiefly as an environmental pollutant that accumulates in animal tissue with resultant pathogenic and teratogenic effects." *Webster's II New Riverside University Dictionary* 912 (1984).

[4/] Texas Eastern has also asserted claims seeking damages for breach of contract against all of its insurers.

On March 11, 1988, Associated Electric & Gas Insurance Services Limited (Aegis) and National Surety Corporation filed Civil Action No. 88-2126 in the United States District Court for the Eastern District of Pennsylvania (Eastern District action) against Texas Eastern, F & C, and Texas Eastern's other CGL insurers. Jurisdiction was based on 28 U.S.C. § 1330(a), 1603(a), and 1605(2) of the Foreign Sovereign Immunities Act (FSIA), because one of the insurers, the Insurance Company of Ireland (one of the London Market Insurers), was an instrumentality of a foreign state.

On March 21, 1988, Texas Eastern filed an action in Texas state court, in Houston (Texas state court action), against all of its insurers.[5/] The Texas state court action was removed to the United States District Court for the Southern District of Texas on the basis of the FSIA and was docketed in that court as Civil Action No. 88-1910.

In May 1988, the Northern District action was transferred by the Judicial Panel on Multidistrict Litigation to this court for consolidation for pretrial purposes with the Eastern District action, pursuant to 28 U.S.C. § 1407; the case was docketed in the Eastern District of Pennsylvania as Civil Action No. 88-5039. The cases were then designated "Texas Eastern Transmission Corporation, PCB Contamination Insurance Coverage Litigation, Case Number MDL 764." In July 1988, the United States District Court for the Southern District of Texas transferred the action pending before it to this district, where it was docketed as Civil Action No. 88-5707. The grounds for the transfer

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[5/] Texas Eastern originally filed this action in New Jersey state court on December 21, 1987. The suit was subsequently dismissed on March 17, 1988, on the ground of *forum non conveniens*.

were not stated, but presumably the transfer was based on 28 U.S.C. § 1404(a). That case has been consolidated for all purposes with MDL 764. (MDL 764 Order No.4, Document No. 23.)

After extensive (and perhaps exhaustive) discovery, the parties filed cross-motions for either partial or total summary judgment. Texas Eastern moved for partial summary judgment on six major issues seeking the following legal rulings: (1) the pollution exclusion in its insurance policies does not bar coverage for long-term pollution; (2) all of its insurance policies were triggered due to the latent nature of the PCB contamination; (3) the Carriers' defenses of late notice and misrepresentation should be stricken; (4) the cleanup costs it has and will incur are recoverable as "damages"; (5) F & C breached its duty to defend Texas Eastern in the underlying lawsuits; and (6) the underlying lawsuits asserted claims for bodily injury, property damage, and personal injury.

The Carriers moved jointly for partial or complete summary judgment on the following issues seeking the following legal rulings: (1) no insurable occurrence ever accrued; (2) the costs incurred by Texas Eastern were not incurred as "damages" because of bodily injury or property damage; (3) Texas Eastern provided late notice of its claims to all Carriers; (4) civil fines and penalties are not insurable as "damages"; (5) the owned property exclusion in Texas Eastern's insurance policies bars coverage for damage to Texas Eastern's own property; and (6) the pollution exclusion in Texas Eastern's insurance policies bars coverage for all costs incurred to remediate the PCB contamination. In addition, twelve of the Carriers individually filed separate motions for partial or total summary judgment in which some of the other Carriers joined. Finally, the Carriers jointly filed several motions to

strike exhibits offered by Texas Eastern in support of its motion for summary judgment.

I held hearings on the summary judgment motions on January 13, 14, and 15, 1992. After consideration of the briefs and the arguments made during the hearings, I have reached numerous conclusions and decisions which are hereafter set forth. I have decided most, but not all, of the issues raised. I have determined that all of the Carriers are entitled to summary judgement on all claims against them because of Texas Eastern's late notice. Other primary issues have been decided in order to avoid extensive further appeals and litigation in the event that a different result occurs on appeal.[6/]

III. SUMMARY JUDGMENT STANDARD

A court shall grant summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c); *Williams v. Borough of West Chester*, 891 F.2d 458, 463-64 (3d Cir. 1989). In a motion for summary judgment, the court may examine evidence beyond the pleadings. The court must always consider the evidence, and the inferences therefrom, in the light most favorable to the nonmoving party. *United States v. Diebold, Inc.*, 369 U.S. 654, 655 (1962); *Tigg Corp. v. Dow Corning Corp.*, 822 F.2d 358, 361 (3d Cir. 1987).

6/. To the extent that I have declined to rule on any outstanding motion in this case, the motion should be considered denied as moot.

The initial burden is on the moving party to demonstrate the absence of a genuine issue of material fact. *First Nat'l Bank v. Lincoln Nat'l Life Ins. Co.*, 824 F.2d 277, 280 (3d Cir. 1987). Once the moving party has satisfied this burden, the nonmoving party must demonstrate that genuine disputes exist concerning each essential element of its case on which it bears the burden of proof at trial. *Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986). For a dispute to be "genuine," a reasonable jury must be able to return a verdict for the nonmoving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248 (1986). If the nonmoving party's evidence is "'merely colorable' or is 'not significantly probative,' summary judgment may be granted" in favor of the moving party. *Equimark Commercial Fin. Co. v. C.I.T. Fin. Servs. Corp.*, 812 F.2d 141, 144 (3d Cir. 1987) (quoting *Anderson*, 477 U.S. at 249-50). In essence, it is my duty to determine whether the nonmoving party has submitted evidence which "presents a sufficient disagreement to require submission to a jury or whether [the evidence] is so one-sided that [the moving party] must prevail as a matter of law." *Anderson*, 477 U.S. at 251-52.

I have gone to great lengths to give Texas Eastern the benefit of every doubt in interpreting the thousands of pages of record evidence submitted by all parties. I have taken this course because the Carriers' summary judgment motion heavily relies on factual findings, while Texas Eastern's summary judgment motion, by its own admission, relies more on interpretations of the law than on express factual findings. In the interest of fairness, I have made extensive

findings concerning the "undisputed facts." *See infra* part VIII.[7/]

IV. MOTIONS TO STRIKE

A. *Motion to Strike Texas Eastern's Motion for Summary Judgment*

The Carriers contend that Texas Eastern's motion for summary judgment is merely a request for hypothetical legal rulings calculated to induce me to reveal my position on particular legal disputes and thereby enable Texas Eastern to better prepare its case for trial. As an example, the Carriers cite Texas Eastern's motion for partial summary judgment on the issue of whether gradual discharge, dispersal, release, or escape of pollutants can be "sudden and accidental" within the meaning of a pollution exclusion clause. In the Carriers' view, Texas Eastern's motion is more appropriate to a Rule 16 conference or a motion *in limine,* where evidentiary rulings are appropriately requested and received.

Texas Eastern responds that seeking legal rulings which narrow the issues for trial are entirely proper in Rule 56 motions, and that its motion need not necessarily allow the court to pronounce final judgment on a particular claim, as long as the court's decision finally disposes of at least some portion of that claim. In addition, Texas Eastern asserts that it need not proffer substantial factual support for its summary judgment motion because it primarily focuses

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7/ In this regard, "[o]nly disputes over facts that might affect the outcome of the suit under the governing law will properly preclude the entry of summary judgment. Factual disputes that are irrelevant or unnecessary will not be counted." *Anderson*, 477 U.S. at 248.

on legal issues which are matters of law for the court to decide and, thus, do not require an extensive factual background.

Federal Rule of Civil Procedure 56(a) expressly entitles a party to move for summary judgment "in the party's favor upon all [claims] or any part thereof." In my view, Rule 56 is broad enough to allow Texas Eastern to move for summary judgment on issues which are crucially important to this litigation, and about which no factual dispute exists. The interpretation of insurance policy language is just such an issue. The Carriers' motion to strike will therefore be denied.

B. *Motion to Strike Certain Evidence Offered by Texas Eastern in Support of Its Motion for Summary Judgment*

The Carriers have also moved to strike certain evidence relied on by Texas Eastern to support its motion for summary judgment. First, the Carriers move to strike exhibits 8-31, 47, [4]8, and 50 offered by Texas Eastern in the Declaration of Laird Hart. Exhibits 8-18 are private third-party complaints filed against Texas Eastern, alleging injuries arising out of PCB contamination, not specifically identified in Texas Eastern's First Amended Complaint. They were the subject of Texas Eastern's motion for leave to file a Second Amended Complaint which I held in abeyance. (Order No. 42, Document No. 443.) In a memorandum and order filed contemporaneously with this opinion, I have denied Texas Eastern's motion for leave to amend its complaint and therefore conclude that evidence of the private third-party complaints is not properly before me. Exhibits 8-18 will therefore be stricken.

Exhibits 19-27 present a more difficult question. Texas Eastern has offered evidence of the drafting history of one

form of a pollution exclusion used in many of the insurance policies at issue in this litigation.[8/] For the reasons set forth in my discussion of the "Pollution Exclusion" issue, *infra* part XII, I have decided that consideration of this evidence is permissible under Texas law and, thus, the Carriers' motion to strike exhibits 19-31 will be denied.

Exhibits 47 and 48 are excerpts from the depositions of Texas Eastern expert witnesses John A. Cherry and Bradford S. Cushing. The Carriers object to this evidence on the ground that the excerpts are insufficient to allow me to determine the experts' qualifications, or the facts and data upon which the opinions are based. Additionally, the Carriers believe that this evidence sets forth mere conclusions and does not offer any evidence of the experts' thought processes or rationale. Texas Eastern has responded by providing some of the deposition transcript missing from its initial proffer. (See TApp.[9/] 222; TApp. 223.) I am satisfied that when considered together with the additional deposition testimony, this evidence is properly before the court and the motion to strike will therefore be denied.

Exhibit 50 consists of two affidavits sworn by Karen Hammerstrom, an EPA employee, which were submitted in support of EPA's enforcement action against Texas Eastern.

[8/] Exhibits 28-31 are documents concerning the intent of various insurance carriers (not necessarily parties to this litigation) regarding the language of the pollution exclusion. For the purposes of this motion, I will consider them as part of the proffered pollution exclusion evidence.

[9/] I will refer to Texas Eastern's Appendix filings as "TApp." and to the Carriers' Appendix filings as "App." Both Appendices were filed in support of the summary judgment motions.

Texas Eastern relies heavily on these affidavits to prove that at least some of its response costs are the direct result of actual or threatened third-party harm to property or persons. Although the affidavits were not created specifically for this litigation, they appear to be reliable and relevant, and appear to satisfy the requirements of Federal Rule of Civil Procedure 56(e). As such, they are properly before me. The Carriers' motion to strike the Hammerstrom Affidavits will therefore be denied.

Second, the Carriers object to any reliance on Texas Eastern's "Statement of General Background Facts" filed contemporaneously with, and in support of, its motion for summary judgment because, in general, it does not cite to record evidence. It is settled law that all evidence relied upon in deciding a motion for summary judgment must be reducible to admissible evidence. Texas Eastern admitted at oral argument that its "Statement of General Background Facts" was not "admissible evidence" and, as such, I have not relied on it in deciding these motions for summary judgment. The Carriers' motion to strike Texas Eastern's "Statement of General Background Facts" will therefore be granted.

C. *Supplemental Motion to Strike*

The Carriers have moved to strike certain additional evidence offered by Texas Eastern. First, the Carriers seek to strike paragraphs 4, 5, 7, and 8 of the Declaration of H. Douglas Church, located at TApp. 191, on the ground that the information contained therein is not based on Mr. Church's personal knowledge. The information in these paragraphs relates to Texas Eastern's historical practices concerning PCB use and containment. The Carriers contend that Mr. Church cannot have personal knowledge of events which occurred before 1985, the date when he first became

responsible for dealing with Texas Eastern's PCB-related problems.

Texas Eastern responds that although Mr. Church does not have first-hand personal knowledge of all the events to which he attested, he acquired personal knowledge by reviewing relevant documents and discussing the issues with senior management[10/] and other personnel from Texas Eastern's Operations, Engineering, Environmental, and Legal departments. (Church Decl., TApp. 191, at ¶ 4.) The Carriers have in turn challenged the quality of Mr. Church's efforts to "get up to speed" on these important issues. (Ins.' Reply in Supp. of Suppl. Mot. to Strike at 4-5.)

Federal Rule of Evidence 602 prohibits a witness from testifying about an issue unless the witness has personal knowledge of the matter. The Carriers complain that Mr. Church's knowledge cannot be personal to him because it was acquired from third parties. This argument proves too much. All perception is inferential to some degree. As the Seventh Circuit recently noted:

> Knowledge acquired through others may still be personal knowledge within the meaning of Fed. R. Evid. 602, rather than hearsay, which is the repetition of a statement made by someone

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10/ Both parties have referred to a generic group of high level Texas Eastern employees as "senior management." Although never defined, I understand this term to refer to employees at Texas Eastern who are, or were, responsible for making important policy and management decisions concerning Texas Eastern's corporate activities. This group is not solely limited to officers and directors, but also includes high level managers responsible for the oversight of Texas Eastern's daily pipeline operations.

> else . . . . Such a statement is different from a statement of personal knowledge merely based, as most knowledge is based, on information obtained from other people.

Agfa-Gevaert, A.G. v. A.B. Dick Co., 879 F.2d 1518, 1523 (7th Cir. 1989).

Mr. Church acknowledges that he relied on various sources to acquire his knowledge of the events to which he attests. He does not, however, offer his statement solely on the authority of those statements, but rather vouches for the statements' truth himself. Mr. Church's alleged reliance on documents distinguishes this case from one in which a declarant relies solely on the "say-so" of third parties. *See, e.g., Kaczmarek v. Allied Chem. Corp.*, 836 F.2d 1055, 1060-61 (7th Cir. 1987). I conclude that the Church Declaration is sufficiently based on personal knowledge and is therefore admissible evidence that can be relied on in deciding these motions for summary judgment.

Next, the Carriers have moved to strike paragraphs 6 and 8 of the Declaration of Steve L. Horton, found at TApp. 194. In paragraph 6, Mr. Horton states that after discussions with environmental representatives of other pipeline companies, it is his understanding that no other pipeline company has been required by EPA or any state authority to install the same source control equipment that Texas Eastern is required to install under the terms of the EPA Consent Decree. (Horton Decl., TApp. 194, at ¶ 6.) The Carriers and Texas Eastern agree that this statement is hearsay if it is offered to prove the truth of the matter, that is, that no other company has, in fact, been required to install the above-mentioned source control equipment.

Texas Eastern contends that this evidence is being offered only to establish what Steve Horton, Texas Eastern's Vice President of Environmental Affairs, believed other companies have been required to do. Without ruling on the relevance of Mr. Horton's opinion, I will deny the motion to strike; however, Mr. Horton's statement is admissible only to establish what he believed has been the practice in the industry.

In Paragraph 8, Mr. Horton states that the residual value of a computer and software, purchased by Texas Eastern exclusively to help carry out the required activities under the Consent Decree, will be little or none when the activities are completed. (Horton Decl., TApp. 194 at ¶ 8.) The Consent Decree involves a ten-year cleanup program. (App. 385 at 16.) Thus, Mr. Horton is merely stating that in his opinion, a computer purchased today will have little value ten years from now.

The Carriers believe that Texas Eastern should offer expert testimony on this issue, or at least lay testimony of someone with expertise in the computer industry. Given the nature of this testimony, I believe that Mr. Horton's duties make him sufficiently knowledgeable about the computer and the work to which it is committed so as to permit his lay testimony to be admitted under Federal Rule of Civil Procedure 701. Of course, the fact that he is not an expert in this area may affect the persuasiveness of his testimony.

The Carriers also move to strike the excerpts of the deposition testimony of Texas Eastern expert Davis L. Ford concerning Texas Eastern's waste management practices. (TApp. 31; TApp. 206.) The grounds for striking the testimony are the same as those asserted in the Carriers' original motion to strike the deposition testimony of experts Cushing and Cherry. Texas Eastern has supplemented its

offer with additional deposition testimony sufficient to allow its admission as evidence. (*See* TE's Opp'n to Suppl. Mot. to Strike at 13-14; Ex. F.) The Carriers' argument that the subject matter of Mr. Ford's testimony is not helpful because it fails to consider Texas Eastern's PCB use goes to the weight, not the sufficiency, of the evidence.[11/]

Finally, the Carriers move to strike TApp. 127 and 129. These exhibits are part of the evidence offered by Texas Eastern concerning circumstances surrounding the drafting of the pollution exclusion which appears in a number of the insurance policies at issue in this case. Having decided that consideration of such evidence is proper under Texas law to help determine whether the term "sudden" is, or is not, ambiguous, I conclude that the evidence is properly before me. For all of these reasons, the Carriers' supplemental motion to strike will be denied in its entirety.

V. CHOICE OF LAW

The parties agree that Texas law applies[12/] to all of the issues in this multidistrict litigation except those concerning the insurability of civil fines and penalties,

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11/ The Carriers' motion to strike Ford's report concerning Texas Eastern's waste management practices, (TApp. 203), on the ground that the report will not be helpful in deciding the motions for summary judgment, will also be denied for the same reason.

12/ I take this opportunity to observe the difficulty and irony of a federal district court judge sitting in Pennsylvania predicting what the Supreme Court of Texas would do if faced with particular questions, given that two of the three cases consolidated in this action originated in Texas and concern activities which primarily occurred there.

where the Carriers contend that the law of the state which imposed the fine or penalty should apply. I will address the choice of law issue regarding civil fines and penalties in my discussion of that issue. (*See infra* part X.C.1.) Otherwise, Texas law will be applied throughout this opinion.

It is axiomatic that the decisions of a state's highest court are the ultimate authority regarding state law. *Connecticut Mut. Life Ins. Co. v. Wyman*, 718 F.2d 63, 65 (3d Cir. 1983). If the state's highest court has not ruled on the issue in question, it is my duty to predict how the state court would rule. *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1167 (3d Cir. 1981). In making these predictions, I have relied, to the best of my ability, on lower Texas state court decisions, well-reasoned authority from other jurisdictions, and other relevant sources.

With respect to my use of sources other than the Texas Supreme Court, I have relied first on lower court decisions from the Texas state courts. Intermediate state court decisions are presumptive evidence of state law. *Commercial Union Ins. Co. v. Bituminous Casualty Corp.*, 851 F.2d 98, 100 (3d Cir. 1988). As the Third Circuit recently stated:

> Although we are not bound in a diversity case to follow decisions of a state intermediate appellate court, we are instructed that such decisions are "not to be disregarded by a federal court unless it is convinced by other persuasive data that the highest court of the state would decide otherwise."

Northern Ins. Co. v. Aardvark Assocs., Inc., 942 F.2d 189, 193 (3d Cir. 1991) (quoting *West v. American Tel. & Tel. Co.*, 311 U.S. 223, 237 (1940)).

I have also relied on decisions from other jurisdictions, as well as other miscellaneous sources, to aid in my predictions in instances where the lower courts have either (1) not decided an issue, or (2) have decided an issue with insufficient rationale to be a good indicator of what the Texas Supreme Court would conclude if faced with a similar question. Although I cannot guarantee that I have predicted correctly, I have relied on my own understanding of the law, and on the insurance and contract principles which Texas courts have historically considered important, to reach the conclusions which follow.

VI. GOVERNING PRINCIPLES OF INSURANCE LAW

A. *Texas Rules of Insurance Contract Construction*

Under Texas law, insurance policies are governed by the same rules of construction which apply to contracts generally. *National Union Fire Ins. Co. v. Hudson Energy Co.*, 811 S.W.2d 552, 555 (Tex. 1991); *Barnett v. Aetna Life Ins. Co.*, 723 S.W.2d 663, 665 (Tex. 1987); *Garrison v. Fielding Reinsurance, Inc.*, 765 S.W.2d 536, 538 (Tex. Ct. App. 1989) (writ denied). "When terms of an insurance policy are unambiguous, they are to be given their plain, ordinary and generally accepted meaning unless the instrument itself shows that the terms have been used in a technical or different sense." *Garrison*, 765 S.W.2d at 538.

When the terms of an insurance policy are ambiguous, a court should apply the construction that favors the insured and permits recovery. *Yancey v. Floyd West & Co.*, 755

S.W.2d 914, 918 (Tex. Ct. App. 1988) (writ denied). A term is ambiguous when the language of a policy is susceptible to more than one reasonable construction. *Yancey*, 755 S.W.2d at 918. "Where the clause of the insurance policy subject to dispute involves exceptions or limitations on the insurer's liability under the policy, even more stringent construction than usual is required." *Id. (citing Glover v. National Ins. Underwriters*, 545 S.W.2d 755, 761 (Tex. 1967)). The court must adopt the insured's construction of an exclusionary clause "as long as that construction is not unreasonable, even if the construction urged by the insurer appears to be more reasonable or a more accurate reflection of the parties' intent." *Hudson Energy Co.*, 811 S.W.2d at 555. However, courts should refrain from creating an ambiguity where none exists. Yancey, 755 S.W.2d at 918. In this regard, "a policy which is otherwise clear is not rendered ambiguous simply because it requires the insured to read the policy thoroughly and carefully." *Labatt Co. v. Hartford Lloyd's Ins. Co.*, 776 S.W.2d 795, 800 (Tex. Ct. App. 1989). Additionally, mere disagreement over the interpretation of an instrument does not make it ambiguous. *Cohen v. Rains*, 769 S.W.2d 380, 389 (Tex. Ct. App. 1989) (writ denied). Indeed, a court must avoid a construction of the policy which renders a portion of the contract meaningless. *Liberty Mut. Ins. Co. v. American Employers Ins. Co.*, 556 S.W.2d 242, 245 (Tex. 1977); *Ideal Mut. Ins. Co. v. Last Days Evangelical Ass'n, Inc.*, 783 F.2d 1234, 1238 (5th Cir. 1986). If no ambiguity exists, parol evidence is inadmissible to create an ambiguity. *Entzminger v. Provident Life & Accident Ins. Co.*, 652 S.W.2d 533, 537 (Tex. Ct. App. 1983). However, in determining whether a contract term is ambiguous, a court should consider the contract terms in light of the surrounding circumstances. *Sun Oil Co. (Del.) v. Madeley*, 626 S.W.2d 726, 731-32 (Tex. 1981).

B. *Texas Rules Concerning the Burden of Proof*

Pursuant to Texas law, the insured bears the burden of establishing that the claimed loss is within the coverage of the policy. *Employers Casualty Co. v. Block*, 744 S.W.2d 940, 944 (Tex. 1988). The insured also bears the burden of proving that it complied with all conditions precedent to coverage. *Trevino v. Allstate Ins. Co.*, 651 S.W.2d 8, 11 (Tex. Ct. App. 1983) (writ refused n.r.e.).

Texas law also requires the insured to prove that the loss does not fall within an exclusion or exception where the insurer pleads such exclusion or exception to coverage. *Sherman v. Provident Am. Ins. Co.*, 421 S.W.2d 652, 654 (Tex. 1967); *American Home Assurance Co. v. Brandt*, 778 S.W.2d 141, 143 (Tex. Ct. App. 1989) (writ denied); *Britt v. Cambridge Mut. Fire Ins. Co.*, 717 S.W.2d 476, 482 (Tex. Ct. App. 1986) (writ refused n.r.e.). I recognize that this is a minority rule, but it appears to be the settled law in Texas.[13/] Finally, if it is determined that the policy provides coverage for only a portion of the insured's loss, the burden of apportioning the damages between covered and noncovered losses is on the insured. *Winn v. Continental Casualty Co.*, 494 S.W.2d 601, 606 (Tex. Civ. App. 1973).

13/ Texas Eastern does not have the burden of proof on the Carriers' affirmative defense of misrepresentation. *See Koral Indus., Inc. v. Security-Connecticut Life Ins. Co.*, 788 S.W.2d 136, 141 (Tex. Ct. App.), *writ denied*, 802 S.W.2d 650 (Tex. 1990). Because I will grant summary judgment to the Carriers on the issue of "Late Notice," I do not reach the merits of the misrepresentation claim.

VII. IMPUTATION OF EMPLOYEE KNOWLEDGE

When individual parties are involved in litigation, the determination of what a party knew or intended is rarely a simple matter. Engaging in a *post hoc* analysis of what an individual was thinking requires powers of clairvoyance which most mortals do not possess. This difficult task is even more formidable when a corporate party is involved. A corporation operates solely through its individual employees. The employees' knowledge and intentions must therefore ordinarily be deemed the knowledge and intentions of the corporation. As Judge Dalton observed:

> A corporation can only act through its employees and, consequently, the acts of its employees, within the scope of their employment, constitute the acts of the corporation. Likewise, knowledge acquired by employees within the scope of their employment is imputed to the corporation. In consequence, a corporation cannot plead innocence by asserting that the information obtained by several employees was not acquired by any one individual employee who then would have comprehended its full import. Rather, the corporation is considered to have acquired the collective knowledge of its employees and is held responsible for their failure to act accordingly.

United States v. T.I.M.E.—D.C., Inc., 381 F. Supp. 730, 738 (W.D. Va. 1974). When dealing with a corporation as large as Texas Eastern, imputation requires an inquiry into the minds of literally thousands of people, and in this case, spanning a time period of three to four decades.

The difficulty of this task does not relieve the parties (or me) of the duty to attempt to reconstruct what Texas

Eastern "knew" at the relevant times. If a corporation were able to escape this imputation of knowledge, it would always be in a position to limit its liability by professing corporate ignorance. At the other extreme, the imputation of every bit of knowledge known to each individual employee—from the Chief Executive Officer to the most recently hired recruit—would likely paralyze a corporation as upper level management attempted to keep informed of all information known to all of the corporation's employees.

Cognizant of this dilemma, courts have created a compromise approach which limits the information imputed to the corporation to that which was learned in the course of an employee's employment-related activities, and which is known by an employee of a sufficient level of corporate responsibility to justify charging the corporation with that knowledge. Texas law is in accord with this approach. Texas Eastern is a corporation and each employee is an agent for the corporation. In accordance with Texas agency law, knowledge which an employee or other agent acquires in the course of employment is imputed to the principal. *Green Tree Acceptance, Inc. v. Holmes*, 803 S.W.2d 458, 460 (Tex. Ct. App. 1991) (writ denied). Texas law makes it clear that this rule of imputation does not depend upon whether the principal actually shares the agent's knowledge, *Williams v. Jennings*, 755 S.W.2d 874, 883 (Tex. Ct. App. 1988) (writ denied), because a principal should not be entitled to the benefits of the agent's services without being charged with the agent's knowledge. *Wellington Oil Co. v. Maffi*, 150 S.W.2d 60, 63 (Tex. 1941).

Texas Eastern is thus charged with the knowledge of its employees as long as that knowledge was gained in the course of the individual employee's employment-related activities. Of course, not all of Texas Eastern's employees will have knowledge of particular events, but this does not

prevent the corporation from being charged with the knowledge of those who do.

Texas Eastern has raised an objection to being charged with the collective knowledge of its many employees for the purpose of determining the intent of the corporation. In *Kern Oil & Refining Co. v. Tenneco Oil Co.*, 792 F.2d 1380, 1386-87 (9th Cir. 1986), *cert. denied*, 480 U.S. 906 (1987), the court concluded that under Texas law, a corporation's subjective intent could not be established by imputing the collective knowledge of its employees. In *Tenneco*, the court reviewed a district court's determination that an overpayment of money was recoverable by the payor corporation, because it was made based on a mistake of fact, and thus was involuntarily made.

Under Texas law, if a party to a contract makes an overpayment, even though it is under no legal obligation to do so, it cannot recover the money if it was voluntarily paid with full knowledge of the relevant facts. *Tenneco*, 792 F.2d at 1386. The payee argued that the corporate party could not claim that its payment was made under a mistake of fact when its employees collectively knew all of the relevant facts. The Ninth Circuit concluded that the collective knowledge could not be imputed because Texas law required that the overpayment be truly voluntary, that is, done intentionally or purposefully or by choice of one's own accord or by the free exercise of the will; the collective knowledge was insufficient to charge the corporation with this action. *Id.*

It is apparent to me that the *Tenneco* court assumed that Texas law required the corporation to subjectively intend to make the overpayment. *Tenneco* is distinguishable from the present litigation because, as will be explained in this opinion, Texas insurance law is not concerned with the

subjective intentions of the insured, but with the objective ones. In an objective analysis, the focus of the inquiry is what the corporation is likely to have known, and not necessarily what the corporation in fact intended. Under these circumstances, I believe the Texas Supreme court would require the corporation to be charged with the collective knowledge of its employees.[14/]

As I previously observed, information known to corporate employees should not be blindly imputed to the corporation. An inquiry should be made as to whether the employee had a sufficient level of corporate responsibility to justify charging the corporation with that particular bit of knowledge. I do not understand this requirement to mean that an employee must have climbed to a particular rung on the corporate ladder, as Texas Eastern has argued, before an employees's knowledge will be imputed. Rather, I believe this to mean that the knowledge must be substantially related to the task which the corporation has assigned the employee to perform. Therefore, information known to an employee which relates to the performance of the employee's job will be imputed to Texas Eastern.

VIII. FACTS

A. *Preliminary Issues*

Both Texas Eastern and the Carriers have submitted versions of the "undisputed" facts. The Carriers initially

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[14/] Other courts have recognized the subjective/objective distinction. *See, e.g., United States v. LBS—New York, Inc.*, 757 F. Supp. 496, 501 n.7 (E.D. Pa. 1990) ("Although knowledge possessed by employees is aggregated so that a corporate defendant is considered to have acquired the collective knowledge of its employees . . . specific intent cannot be aggregated similarly.")

filed the "Insurers' Statement of Material Facts As To Which No Genuine Issue Exists" (SOF). Texas Eastern responded to the Carriers' filing with "Texas Eastern's Response To The Insurers' Statement Of Material Facts As To Which No Genuine Issue Exists" (TRSOF), in which Texas Eastern either disputed the Carriers' assertions or admitted them. Texas Eastern contemporaneously filed its own version of the material facts in "Texas Eastern Statement Of Facts" (TSOF). Finally, the Carriers' filed a response to the TRSOF.

The Carriers' response to the TRSOF raised several important issues. First, the Carriers objected to the filing of the TSOF *after* Texas Eastern had filed its motion for summary judgment. In the Carriers' view, Texas Eastern bore the initial burden of "identifying those portions of the 'pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any,' which it believe[d] demonstrate the absence of a genuine issue of material fact." *Celotex*, 477 U.S. at 323. By failing to meet this burden in its initial filing, the Carriers contend that Texas Eastern gained an unfair advantage by waiting until the Carriers had "tipped their hand before it too committed itself." (Ins.' Reply to TRSOF at 2 n.1.)

The Carriers are clearly correct in their assertion that a party seeking summary judgment must file, in support of its motion, a statement of the facts which is supported by record evidence. However, this is not a case where a party as *failed* to file such a statement, but one in which a party has failed to file its statement contemporaneously with its original motion.

Texas Eastern filed a response to the SOF, and its own TSOF, on September 9, 1991, almost two months after its initial filing of the summary judgment motion, filed on July

12, 1991. There is no dispute that taken together, the TRSOF and the TSOF satisfy the *Celotex* requirement of identifying those portions of the pleadings which Texas Eastern believes demonstrate the absence or existence of a genuine issue of material fact.

In light of the voluminous filings in this case, I conclude that while it would have been more appropriate for Texas Eastern to have filed its statement of facts with its summary judgment motion, the Carriers have not been significantly prejudiced by Texas Eastern's late filing. All of the filings in this case were made pursuant to a Case Management Order, which clearly sets forth the timetable for opposition and reply briefs. Texas Eastern filed its statement and response well within the allowable time. For these reasons, I will consider both the TRSOF and the TSOF in the disposition of these motions.[15/]

The second issue raised by the Carriers in their reply brief is the sufficiency of the record evidence upon which Texas Eastern relies to "dispute" many of the Carriers' factual assertions. Having reviewed Texas Eastern's responses, I conclude that the Carriers have raised numerous meritorious objections. Because many of the factual assertions are immaterial to my decision on the pending motions, I will not restate each of these objections in detail.

In the factual section which follows, I have set forth what I conclude to be the "undisputed" facts. These facts

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[15/] The TSOF should not be confused with Texas Eastern's "Statement of General Background Facts" which I have previously concluded cannot be relied on because it lacks sufficient references to record evidence. (*See supra* pp. 12-13.)

will be relied upon in deciding the cross-motions for summary judgment. Many of the facts have been admitted by Texas Eastern or by the Carriers. Some of the facts, however, have been disputed by the parties, but after a thorough investigation of the record evidence, the disputes have been found not to be "genuine." The facts below reflect many of the Carriers' above-mentioned objections. In many instances, but not all, I will discuss the reasons for my conclusion that no genuine dispute exists.

B. *Factual Background*[16/]

1. *Texas Eastern's Corporate History*

Texas Eastern was incorporated in Delaware on January 30, 1947. In that year, it acquired the War Emergency Pipeline from the United States Government and

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16/ In each paragraph of the TRSOF, Texas Eastern repeated the Carriers' original allegation as it appeared in the SOF, and then stated its response. My citations to the TRSOF refer not to the Carriers' statements, but to Texas Eastern's. For example, if Texas Eastern did not dispute a proposition, or disputed it on different grounds, a citation to that paragraph in the TRSOF refers to Texas Eastern's acceptance of the proposition. Sometimes Texas Eastern claims to have disputed a proposition, but I find that the only dispute raised by Texas Eastern is immaterial. In that situation, I have treated the fact as undisputed by Texas Eastern, and have therefore included a TRSOF cite as an admission by Texas Eastern that the fact is indeed undisputed. On certain occasions, when Texas Eastern's dispute is material, I have cited to the TRSOF for the text of Texas Eastern's response itself. When I wish to cite to a fact alleged to be undisputed by the Carriers, but materially disputed by Texas Eastern, I have cited to the SOF instead. Likewise, when I wish to cite to a fact alleged to be undisputed by Texas Eastern, I have cited to the TSOF. In short, any citation beginning with "T" can be understood to mean that Texas Eastern has agreed to, or has not materially disputed, the proposition stated.

converted it from liquid service to a natural gas pipeline system. (TRSOF ¶ 1.)

The Texas Eastern Corporation was incorporated in Delaware in 1976. It was incorporated as the parent holding company of Texas Eastern and other subsidiaries. In 1989, the Texas Eastern Corporation was acquired by Panhandle Eastern Corporation. The real party in interest in this litigation is Texas Eastern, not its parent holding company or any of the unidentified subsidiaries, and I will refer solely to Texas Eastern in this opinion.

By 1987, Texas Eastern operated a natural gas transmission network which included as its primary operation a pipeline approximately 9,500 miles in length from supply areas in Texas, Louisiana, and the Gulf of Mexico to the New York Metropolitan area.[17] (TRSOF ¶ 5.) Approximately 65 stations at various locations along the pipeline system used turbine-driven centrifugal compressors to increase the pressure of the natural gas being transmitted. (TRSOF ¶ 2.)

2. *Texas Eastern's Operational History*

In late 1957 or early 1958, Texas Eastern identified a problem with the lubricating oil used at its centrifugal compressor stations. It was suspected that the extreme heat of the turbines caused the oil to ignite; the ignitions caused a number of dangerous fires. (TSOF ¶¶ 4, 5.) In response to the fires, Texas Eastern conducted an extensive study of

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[17] The pipeline passes through, among others, the following states: Texas, Louisiana, Mississippi, Arkansas, Alabama, Tennessee, Kentucky, Missouri, Illinois, Indiana, Ohio, West Virginia, Pennsylvania, Maryland, and New Jersey. (TE's First Am. Compl. at ¶ 39.)

commercially available fire-resistant lubricants and, in 1958, selected Monsanto Chemical Corporation's (Monsanto) OS-81[18] as a replacement. (TRSOF ¶¶ 6, 8.) The lubricant (apparently almost all PCB) had PCB concentrations of approximately 88%-90%. (TRSOF ¶ 13.)

Texas Eastern immediately began installing the new lubricant in some of its turbine-driven centrifugal compressors. (TRSOF ¶¶ 17, 18.) By 1970, Texas Eastern had installed the lubricant in 24 compressor units, at 19 compressor stations, located in approximately 8 or 9 states. (TRSOF ¶ 19.)

Texas Eastern used the Monsanto lubricant in its centrifugal compressors as both a lubricant and a seal oil. (TRSOF ¶ 31.) As a seal oil, the lubricant provided a pressurized seal against the natural gas compressed inside the compressor cases, which prevented the natural gas from escaping into the atmosphere. (TRSOF ¶ 32.) The centrifugal compressors were designed as "closed systems" and should therefore have operated without a noticeable leakage of oil. (TRSOF ¶ 35; TSOF ¶¶ 31-33.) Texas Eastern was aware, however, that the lubricating oil was "used" or "consumed" by the compressors, thereby requiring a routine replacement of the oil. (TRSOF ¶¶ 37, 38.) Texas Eastern prepared and maintained a "Compressor Department Annual Report" which detailed the amount of

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[18] The lubricant purchased from Monsanto has been known in its various formulations as OS-81 (beginning in 1958), MCS-153 (beginning in 1961), and Turbinol-153 (beginning in 1970). (TRSOF ¶ 13.) All appear to have contained high PCB concentrations.

lubricant consumption at each compressor station. (TRSOF ¶ 37.)[19]

The parties vigorously dispute the reason for the large consumption of the lubricant oil. Texas Eastern contends that many senior employees believed that most of the lost lubricant was simply vaporized by the extreme heat of the turbine-driven centrifugal compressors, in the same way that oil is consumed in an automobile. (TSOF ¶ 31.) The Carriers concede that some of Texas Eastern's employees may have believed that lubricant was being consumed in this manner. However, the Carriers have produced evidence which establishes that key Texas Eastern personnel were aware that the compressor system was designed in a manner that all but guaranteed that some lubricant would leak out of the compressors, come into contact with the natural gas, and enter into the pipeline.[20]

For example, Texas Eastern's Superintendent of Compressor Stations, E.C. Riall, testified that he was aware, at the time he was working for Texas Eastern, that the passage of some amount of lubricant into the compressor case was "an inherent design of centrifugal compressors." (Dep. of Eugene Riall, App. 56 at 186). *See also* App. 14 at 358-59 (deposition testimony of Texas Eastern's Assistant Chief Engineer, Conrad W. Marvin,

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[19] The compressors consumed a substantial amount of lubricant. For example, of the 210,713 gallons of lubricant purchased from Monsanto, Texas Eastern's compressors consumed 175,856 gallons of the lubricant from 1958 to 1977. (TRSOF ¶ 39.)

[20] Texas Eastern admits that there was a large leakage of lubricant from the compressor units into the natural gas pipeline. The only material dispute concerns when Texas Eastern became aware of this fact.

stating that Texas Eastern understood that the seal oil leaked as early as 1949).

There were occasional accidents and malfunctions involving the compressor unit systems, which explains how some of the lubricant was lost; the vaporizing of lubricant provides a second potential explanation. These explanations are insufficient, however, to explain the disappearance of the majority of the used lubricant, and Texas Eastern has offered insufficient evidence to refute the testimony of its own employees. Those Texas Eastern employees who testified that they understood that the seal oil system was not working perfectly and that a significant amount of lubricant was thereby lost, must therefore be believed.[21/]

Texas Eastern's contention that the compressor seal systems were designed as "closed systems" with no leakage or "consumption" of lubricant oil is immaterial because there is no credible evidence which tends to establish that all Texas Eastern employees were working under this assumption or, more importantly, that this assumption was correct. Texas Eastern's reliance on the fact that its senior management was unaware of the extent of the seal oil failures, and the amount of oil which leaked into the pipeline, is equally unavailing. Texas Eastern's managers, charged with running the individual compressor stations, knew that lubricant oil was escaping down the pipeline and Texas Eastern is therefore charged with that knowledge.

21/ Further supporting this conclusion is the fact that Texas Eastern tested at least one epoxy, used to coat the inside of the natural gas pipeline, for compatibility with OS-81, and replaced the "O" rings in its compressor units with ones compatible with the Monsanto lubricant. (TRSOF ¶¶ 46, 47.) Texas Eastern admits to taking these measures as a precaution to guard against the possibility that lubricant would escape into the pipeline. (TRSOF ¶ 47.)

Texas Eastern cannot hide behind its senior management's ignorance of the basic aspects of its compressor stations' daily operations. For all of these reasons, there is no material dispute that Texas Eastern was aware, for many years, that some of the lubricant oil was escaping from the turbine-compressors and entering the natural gas pipeline.

The centrifugal compressors operating on Texas Eastern's natural gas pipeline were routinely started-up and shut-down during the course of normal pipeline operation. (TRSOF ¶ 48.) During start-up, the compressor was purged of air and pressurized, and natural gas present in the compressor case was vented to the atmosphere through the compressor vent stacks. (TRSOF ¶ 49.) During shut-down, the compressor case was depressurized and the natural gas within the compressor case was again vented to the atmosphere. (TRSOF ¶ 50.)

During start-up, any lubricant present in the compressor case was vented into the environment from the compressor vent stacks along with the air and natural gas. During shut-down, any lubricant present in the compressor case was similarly vented along with the natural gas. Although the parties disagree as to whether Texas Eastern was aware at the times relevant to this litigation that lubricant was being vented and lost into the environment in this manner, they do agree that at least some of Texas Eastern's operational employees understood that lubricant

was sometimes being vented into the air (and settling on the ground) along with the natural gas. (TRSOF ¶ 54.)

Pipeline liquids, consisting of hydrocarbon distillates[22] and water, routinely entered Texas Eastern's natural gas pipeline. (TRSOF ¶ 57.) The lubricant that escaped from the compressor cases and entered the pipeline mixed with those fluids already present in the pipeline. From the time it began operations in 1947, Texas Eastern used its compressor stations as sites for the collection, removal, storage, and disposal of those pipeline liquids.[23] (TRSOF ¶ 56.) Texas Eastern primarily used two methods for the removal of pipeline liquids: gas/liquid separation equipment (scrubbers and strainers) and cylindrical devices known as "scrapers" or "pigs."[24] (TRSOF ¶ 63.)

The liquids accumulated by scrubbers, strainers, scrapers, and pigs were routinely[25] discharged into

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[22] Pipeline distillates can be harmful to the human body and to vegetation depending on the nature and extent of the exposure. It was therefore undesirable to allow the distillates to come into contact with property on which vegetation growth was desirable. In this regard, Texas Eastern personnel considered pipeline liquids to be pollutants if they escaped in undesirable quantities from their containment pits.

[23] This was no small task. Texas Eastern removed twenty million gallons of liquid from its pipeline during the thirty year period 1957 through 1987. (TRSOF ¶ 62.)

[24] Pigs are shafts with attached brushes and/or rubber cups that, when inserted into a pipeline segment, make contact with the pipeline wall, and push the liquids forward to collection areas in the pipeline.

[25] There is some dispute as to whether Texas Eastern's personnel "routinely" dumped pipeline liquids within the scope of their employment or merely dumped the liquids "as needed." This is a

(continued...)

unlined earthen pits at the compressor stations.[26] (TRSOF ¶¶ 71, 77; TSOF ¶ 74.) The PCB-based lubricant, carried along in the pipeline liquids, was thereby discharged into the unlined earthen pits. (TRSOF ¶ 73.)

Texas Eastern used its pits to collect, contain, and prevent the escape of pipeline liquids to other areas including neighboring third-party property. (TSOF ¶ 74.) The pipeline liquids were generally burned, but in some cases were hauled away, or were applied by Texas Eastern employees to kill weeds or control dust on dirt roads.[27] (TSOF ¶ 75; TRSOF ¶¶ 84-86, 101, 106.) Texas Eastern personnel understood that some of the liquids were absorbed into the ground, but it is disputed whether this was an intended method of disposal or simply a fact about which Texas Eastern was aware. (*See* App. 113, at 002021610;

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[25](...continued)
distinction without a difference. It is clearly established that Texas Eastern personnel repeatedly dumped pipeline liquids into the unlined earthen pits whenever the responsibilities of their jobs required such dumping.

[26] The pits were generally about ten to thirty feet in diameter on isolated portions of the compressor station sites. The pits were typically lined with clay or dug in hard, compact, non-porous ground. (TSOF ¶ 77.) The pits were ordinarily surrounded by an earthen berm, made from the material excavated in the process of digging the pit, that served as a precaution against accidental overflow. (TSOF ¶ 78.)

[27] Although Texas Eastern disputes the Carriers' contention that Texas Eastern "disposed" of its pipeline liquids into the pits, there is no doubt that in most instances Texas Eastern intended the pits to be the pipeline liquids' final resting place. For example, at some compressor station locations, the earthen pits had built-in pilot lights that automatically ignited any incoming liquids. (TSOF ¶ 79.) No evidence has been produced to explain what saleable or other value existed for the burnt remains of Texas Eastern's pipeline liquids.

App. 118, at 002021192; App. 119 at 002021024—All three Effluent Discharge Survey reports indicating that absorption of pipeline liquids was known to occur.)

The pits proved to be imperfect containment vessels, however, and during the period between 1958 and 1976, Texas Eastern was aware of instances where pipeline liquids escaped from the pits and migrated onto other areas of Texas Eastern's property or the property owned by neighboring third parties. (SOF ¶¶ 114-152; TSOF ¶¶ 52-62.) In 1973, Texas Eastern voluntarily conducted an "Effluent Discharge Survey" of all compressor station facilities. (TRSOF ¶ 132.) The purpose of the study was to identify potential problem areas by soliciting information from each compressor station location that had, or may have had, effluent discharges, particularly those that may have had liquids drain off Texas Eastern's own property. (TRSOF ¶ 133.)

The survey results indicated that some of the lubricant used in the compressors was migrating from Texas Eastern's property to the property of third parties. (TRSOF ¶¶ 135, 137, 143-45.) These instances were considered isolated occurrences and were generally remedied once Texas Eastern was made aware of their existence. The survey also establishes that Texas Eastern was fully aware of both potential and actual occurrences of off-site migration of pipeline liquids, and once Texas Eastern understood that the pipeline liquids contained PCBs, Texas Eastern should have been aware of the potential for off-site PCB migration.

Although Texas Eastern personnel were warned of the potential for overflow from the pits due to rainfall, and were instructed to guard against it, Texas Eastern was aware that overflows occasionally occurred. (TRSOF ¶

147.) Texas Eastern was also aware of the potential for movement of the pipeline liquids from the compressor stations to other property from various sources, including the earthen pits and the pig receivers. (TRSOF ¶ 151.) In 1975, Texas Eastern drafted a "Water Pollution Prevention and Control Plan" for the purpose of controlling this undesirable spread of pipeline liquids. (TRSOF ¶¶ 150-51, 231-32.)

3. *Texas Eastern's Knowledge of PCBs in its Lubricant*

In February 1970, Monsanto sent correspondence to its customers alerting them to an increasing concern over the adverse environmental impact of Monsanto's PCB-containing products and Monsanto's intention to reformulate those products. (SOF ¶ 183.) Monsanto recommended that PCBs no longer be used in applications which would lead either directly or indirectly to the contamination of food and water supplies for humans or animals. (TRSOF ¶ 184; TSOF ¶ 12.) Following its own advice, Monsanto terminated its sale of certain products containing PCBs to certain of its customers.

After informing its customers of the decision to terminate the sale of certain products, however, Monsanto published a promotional booklet about Turbinol-153, stating that it had a history of safe use as both a lubricant and control fluid in commercial pipeline gas turbines. (TSOF ¶ 14; App. 27 at 2.) Texas Eastern was aware of this booklet. (TSOF ¶ 14.) On January 7, 1972, however, Monsanto proposed that Texas Eastern sign a hold harmless agreement promising to indemnify Monsanto for any future liability arising out of the sale of Turbinol-153 after January 15, 1972. (TRSOF ¶ 187; App. 186.) Monsanto further informed Texas Eastern that because Turbinol contained

"major amounts" of certain polychlorinated biphenyl products (PCBs), it would no longer sell any Turbinol to Texas Eastern after June 30, 1972. (TRSOF ¶ 189; App. 186.)

Texas Eastern elected not to sign the hold harmless agreement, but it did attempt to purchase Monsanto's remaining stock of lubricant oil available for sale before the January 15, 1972 deadline. (App. 190.) Monsanto apparently refused to sell Texas Eastern any more PCB-based lubricant. (*Id.*) In May 1972, Texas Eastern began a program referred to as the "phase-out" or "change-out" program to replace the PCB-based lubricant with non-PCB-based oil. (TRSOF ¶ 199.)

4. *The Change-Out Program*

Because Turbinol-153 and the replacement oil were compatible, the change-out program did not necessarily require Texas Eastern to flush the turbine driven compressors of the PCB-based lubricant and replace it with non-PCB-based oil. (App. 194 at 3.) Complete flushing was advisable from an ecological standpoint, however, presumably because anything less would have resulted in Texas Eastern's continued use of a lubricant containing PCBs. On April 12, 1972, Texas Eastern chose the replacement for Monsanto's Turbinol-153. (App. 214 at 2.) In May 1972, Texas Eastern began installation of the replacement lubricant. (*Id.*)[28/]

[28/] Once removed from a compressor unit, the PCB-based oil was used for "make-up" (replacement) in those units which continued to use the PCB-based lubricant. (TSOF ¶ 24.) Three units were changed out in 1972, and an additional three units were changed out in 1973. (TSOF ¶¶ 24, 25.)

The speed with which Texas Eastern conducted its change-out program is a subject of dispute between the parties. The Carriers contend that the speed depended upon the rate of consumption of the PCB-based oil in the turbine compressor units. (SOF ¶ 203.) Texas Eastern responds that it intended to convert its compressors to non-PCB-based lubricants as quickly as possible, but that it was restrained by the technical difficulty of the change-out and the difficulty of finding an appropriate replacement lubricant. (TSOF ¶¶ 21-26.)

Ultimately, the rate at which Texas Eastern completed the change-out probably depended on all of these factors. There can be no dispute, however, that Texas Eastern was, at least initially, concerned with utilizing as much of the its remaining inventory of Turbinol-153 as it could. (Dep. of Walter Woods, App. 42 at 754-59; App. 195 at 010028581.) To achieve this end, Texas Eastern made its change-out decisions based, at least in part, on the lubricant consumption rates of various compressor stations—choosing to change those compressor stations with higher consumption rates last. (App. 203; Dep. of Eugene Riall, App. 56 at 109-12; App. 200.)

As early as August 1972, Texas Eastern was aware of evidence indicating that a break-down product of the Monsanto Oil was in the compressor units and the pipeline, contaminating the non-PCB-based replacement lubricant. (App. 213.) In July 1976, Texas Eastern's testing confirmed that some of the replacement lubricant was contaminated with PCBs. (TRSOF ¶ 223.) In the same year, one Texas Eastern employee wrote a memorandum in which he indicated that he understood that using the PCB lubricant meant that the oil was being spread throughout the entire pipeline system. (App. 211.) This evidence indicates that Texas Eastern was on notice, during this time period,

that the change-out program had not completely solved its PCB lubricant problems.

Throughout the change-out program, Texas Eastern continued to dump pipeline liquids into the unlined earthen pits at its compressor stations. Texas Eastern was aware that the amount of liquids accumulating in its pits was increasing and raised some concerns as to whether the pits were adequate containment vessels. (App. 221.) One explanation for this increase is that Texas Eastern's management discouraged burning in the disposal pits as early as 1972, (App. 220 at 010020659), and implemented a formal "no burn" policy in 1975. (App. 221; TRSOF ¶ 235.) This required Texas Eastern to rely more heavily on evaporation and siphoning to reduce the amount of liquid in the pits. (App. 221)

By July 11, 1975, Texas Eastern's Operating Department abandoned the policy of disposing pipeline liquids into the unlined pits in order to comply with environmental regulations being established by the various states in which Texas Eastern operated. (App. 223.) Subsequently, Texas Eastern commenced a program to install diffuser tanks at the compressor stations to replace the unlined earthen pits as the receptacles for the pipeline liquids. The replacement program was substantially completed by 1985. (TRSOF ¶ 237.) After a pit was replaced by a diffuser tank, the pit was backfilled by pushing in the surrounding berm with a bulldozer and grading the area to its natural contours. (App. 165 at 12.)

5. *Tracking Environmental Legislation*

In the early 1970s, PCBs became generally known as a potential hazard to human health and the environment. Not surprisingly, Congress and numerous state legislatures

moved to regulate the uses of the toxic substance. Texas Eastern was aware of this legislative activity. (TRSOF ¶¶ 241-47.) Acting pursuant to the authority granted it by the Toxic Substances Control Act (TSCA),[29] EPA promulgated a final rule on May 31, 1979, which, *inter alia*, prohibited the use of PCBs in concentrations above 50 parts per million (ppm), except in totally enclosed systems. (App. 279, 44 Fed. Reg. 31544.) The rule, however, authorized the continued use of PCBs above the 50 ppm limit in natural gas pipeline compressors until May 1, 1980, in systems which were not totally enclosed. (App. 279, 44 Fed. Reg. 31551.)

In September 1978, Texas Eastern understood that it was impermissible to dispose of liquid mixtures of PCBs in excess of 500 ppm in landfills. (App. 236.) The only permissible disposal method was to incinerate the waste in an EPA approved incineration facility. (TRSOF ¶ 250; App. 236.) Employees at Texas Eastern were also aware of EPA requirements regarding PCB storage facilities. (TRSOF ¶ 254; App. 237.) With these rules in mind, Texas Eastern constructed and used storage buildings, at various compressor stations, to store drums containing the PCB-based lubricant. (TRSOF ¶ 255.) Due to the danger of storing large amounts of petroleum oil on its property, Texas Eastern advised its first-party property insurers, in December 1978, about the storage buildings, but did not give notice to its third-party liability carriers. (App. 242; App. 245; TRSOF ¶ 258.)

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[29] 15 U.S.C. § 601 *et seq.*

6. *PCB Contamination in the Natural Gas Pipeline*

In January 1981, Texas Eastern learned that PCBs were detected in a Long Island residential gas meter. (TRSOF ¶ 263.) A subsequent investigation by Texas Eastern, in a 36 location sampling program, conclusively revealed that Texas Eastern's pipeline liquids were contaminated with PCBs. (App. 276.) The Brooklyn Union Gas Company informed Texas Eastern that it would seek, from Texas Eastern, reimbursement of the costs incurred for cleaning up the PCB contamination, (App. 267), and Texas Eastern provided notice of these claims to Aegis, its excess liability carrier, (TApp. 148), but not to its other third-party liability insurance carriers. (TRSOF ¶ 266.)

As a result of Texas Eastern's testing and the discovery of PCBs in its pipeline liquids, Texas Eastern met with EPA officials, on March 27, 1981, to discuss Texas Eastern's remedial plans. (App. 277.) According to a Texas Eastern internal memorandum, Texas Eastern's Vice President of Operations, F.L. Cohagan, told EPA's John Seitz that Texas Eastern planned to test all of its pipeline liquids for PCBs before disposal, and that Texas Eastern would use accumulator tanks (instead of open pits) for collecting liquids at the compressor stations. (*Id.*) J. Clifton Williams, Texas Eastern's Director of Technical Services, testified at his deposition that Mr. Cohagan also explained to Mr. Seitz that the pits would continue to be used until all of the accumulator tanks had been installed. (Dep. of J. Clifton Williams, TApp. 7 at 644-48, 659-60.)

By letter dated May 27, 1981, EPA informed Texas Eastern that it was establishing a four-part program to reduce the risk from PCBs in gas pipeline systems: (1) to ensure the proper handling of PCBs removed from the

pipeline, (2) to obtain information on ways to prevent further movement of PCBs into other systems, (3) to implement the best option identified in step two, and (4) to obtain information on the possible methods for removing any remaining PCBs from the system. (App. 282.) Subsequently, Texas Eastern sent its response to EPA's letter outlining its proposed plan for handling the PCB liquids in its pipeline. (App. 281.) Texas Eastern and EPA agreed upon a plan for the cleanup in late 1981 or early 1982. (TRSOF ¶ 284.)

7. *PCB Cleanup*

On July 23, 1982, EPA instituted an enforcement proceeding against Texas Eastern pursuant to the Toxic Substances Control Act alleging that Texas Eastern was using PCBs in violation of 15 U.S.C. § 2614(1) & 40 C.F.R. § 761.20(a). (App. 287.) The gravamen of the violation was Texas Eastern's continued use of compressor fluids containing PCB concentrations exceeding 50 ppm in its turbine driven compressors. (*Id.*) On August 3, 1982, Texas Eastern entered into a Consent Order, Consent Agreement, and Compliance Schedule with EPA addressing the use of lubricant contaminated with PCBs in its pipeline system. (App. 288; App. 289; App. 290.) Texas Eastern did not provide notice of these activities to its third-party liability carriers.

The agreements, both formal and informal, entered into by Texas Eastern and EPA did not cover the remediation of the unlined earthen pits. Texas Eastern does not dispute the fact that at some of its compressor stations, Texas Eastern continued to use the pits to "dispose," or at a minimum, to "temporarily store," (TSOF ¶ 86), pipeline liquids known by Texas Eastern to be contaminated with residual PCBs. In fact, Texas Eastern admits that it was

necessary to continue using the pits until appropriate accumulator tanks could be installed at all of the compressor station sites known to contain contaminated lubricant, pipeline liquids, or both. (Dep. of J. Clifton Williams, TApp. 7 at 644-48, 659-60.)

For example, as of August 27, 1982, Texas Eastern's St. Francisville, Louisiana station received pipeline liquids into its pits containing PCBs in a concentration ranging from 7 ppm to 2700 ppm. (App. 293.) In addition, sampling in pits on its Transwestern Pipeline System (a wholly owned subsidiary of Texas Eastern) in Corona, New Mexico made Texas Eastern aware that PCBs were present at those sites and had migrated into the soil from an unlined earthen pit. (TRSOF ¶ 298.) Although Texas Eastern contends that it was not aware of any off-site migration of the PCBs, the estimated cost of "decontamination" at the Corona compressor station alone was in excess of $ 500,000. (App. 298.) After Texas Eastern attempted to remediate the Corona site in 1983, it was apparent to Texas Eastern employees responsible for the remediation attempt that the PCBs had migrated from the lubricant into the sides and bottom of the disposal pit. (TRSOF ¶ 298.)

As Texas Eastern gradually stopped discharging pipeline liquids into its pits, it routinely backfilled them with earthen fill. (App. 165 at 12.) At Texas Eastern's St. Francisville, Louisiana; Union Church, Mississippi; and Clinton, Mississippi stations Texas Eastern closed the pits by (1) skimming the oil off the surface of the pipeline liquids and carting it away for incineration, (2) draining the water out of the pit and filtering it for low level PCB contamination, (3) solidifying PCB sludge by mixing it with fly-ash, and (4) installing a plastic cover to prevent any percolation through the solidified mass. (App. 305.) The

pits were then marked so that they could be easily located at a later date. (App. 2 at 88-89.)

On November 29, 1984, EPA Region 9 issued a civil administrative complaint against the Transwestern Pipeline Company (Transwestern) for improperly marking, storing, and disposing of PCB-laden waste oils into unlined earthen pits in Arizona. (App. 307.) At this time, Texas Eastern was completing, or had completed, the sale of Transwestern to Houston Natural Gas (HNG). (Dep. of Bolivar Andrews, App. 309 at 159-61.) In April 1985, Transwestern entered into a Consent Agreement and Final Order with EPA. (App. 306.) Around this time, Texas Eastern entered into an agreement with HNG to amend the contract of sale so that Texas Eastern would bear some financial responsibility for the costs of remediating PCBs from pits in the Transwestern System. (App. 311.) Texas Eastern did not provide notice of this agreement to its third-party liability carriers.

As a result of the Transwestern Complaint, Texas Eastern undertook a survey of its pit use along its entire pipeline system. (TRSOF ¶ 312.) In August 1985, EPA issued a Notice of Non-Compliance to Texas Eastern's Delmont, Pennsylvania compressor station for violations of TSCA regulations concerning the marking, storage, disposal, and record keeping of PCBs. (App. 317.) A subsequent meeting was held with EPA on August 29, 1985, and Texas Eastern advised EPA that it was preparing to close the earthen pits formerly used to contain PCB-laden pipeline liquids at stations where the pits had been replaced by liquid separators and/or accumulator bottles. (App. 319.) EPA advised Texas Eastern that it should submit information regarding the location, site, predominant usage, current status, and closure date of some of the pits. (TRSOF ¶ 320.) Presumably, Texas Eastern then understood that it

could no longer use the pits to hold, even temporarily, any pipeline liquids containing more than 50 ppm of PCBs.

Texas Eastern admits that it realized, by late 1985, that it would have to formulate a remediation plan for the unlined earthen pits—something it had previously believed to be unnecessary. (Dep. of Howard Homeyer, App. 315 at 134.) To facilitate the creation of the plan, Texas Eastern hired Roy F. Weston, Inc. (Weston), a national environmental consulting firm, to determine the nature and extent of the PCB contamination around the pits. (App. 323.) Simultaneously, Henry H. King, President of Texas Eastern, consulted with Steve Mulliken, Director of Texas Eastern's Risk Management Department, regarding the possibility of insurance coverage for the earthen pit remediation. Mr. King reached the initial conclusion that CGL insurance policies would not cover the estimated 40 to 50 million dollars that the remediation program would cost. (TRSOF ¶ 325; App. 324; Dep. of Henry King, App. 318 at 121-22.)

In November 1985, Texas Eastern employees met with employees of Weston to discuss Weston's work schedule. (TRSOF ¶ 333.) At this time in late 1985, the manager of Texas Eastern's Environmental Protection Department, Robert Salzer, understood that many of the pits and landfills at the compressor stations were not in compliance with federal regulations regarding the storage and disposal of PCBs. (Dep. of Robert Salzer, App. 105 at 49-50, 453-63.)

8. *The Results of Weston's Survey*

In January 1986, Weston and Texas Eastern held a progress meeting to discuss the results of Weston's initial

sampling of six compressor station sites.[30] (App. 340.) On February 18, 1986, Weston provided Texas Eastern with a draft report entitled "Compressor Station Disposal Pit Investigation." (App. 341.) This report included the results of Weston's initial six-site survey. (*Id.*) Weston concluded that

> [b]orings drilled adjacent to but outside of the pit perimeters indicated very low to no PCB content, and, thus, minimal migration of PCBs from the pits. However, the PCB presence in the drainage swales and surface water bodies indicates that the potential for off-site migration exists.

(App. 341 at 001363937.) The report did not, however, conclusively find evidence of off-site migration although reasonable minds might differ about this characterization of the report. (Dep. of Bradford Cushing, TApp. 106 at 294, 374-75, 539, 670-71.)

In the months following the delivery of Weston's initial report, Texas Eastern's senior management received a number of general briefings concerning the PCB "situation." Examples include (1) a February 27, 1986 Board of Directors meeting at the Ocean Reef Club in Key Largo, Florida, (App. 343), (2) a February 28, 1986 Public Policy Committee meeting, (Dep. of Fred Wichlep, App. 344 at 213-18), and (3) a March 5, 1986 meeting of the Executive

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[30] The survey was conducted at six compressor station sites and included eight pits. The parties have refereed to the study as both the "six" and the "eight" site survey, and I will refer to it as the "six-site survey."

Committee of the Board of Directors, (App. 345). In late April 1986, Texas Eastern's senior management was briefed about the estimated cost and duration of a pit remediation effort. (App. 347; App. 348.)

On April 1, 1986, EPA requested additional information from Texas Eastern regarding its use of earthen pits located at various compressor stations. (TRSOF ¶ 345.) Texas Eastern responded on April 25, 1986, and provided EPA with a final version of Weston's pilot program report (six-site survey) dated April 21, 1986. (TRSOF ¶ 348.) In Texas Eastern's April 25, 1986 letter to EPA, it admitted that it had used the earthen pits for the collection of pipeline liquids at certain compressor stations until the fall of 1985. (TRSOF ¶ 349.)

Texas Eastern subsequently met with EPA officials on April 30, 1986, to discuss the status of Weston's pit investigation, and to discuss a draft "action plan" prepared by Texas Eastern for the remediation of the compressor station sites. (TRSOF ¶ 350.) Texas Eastern represented to EPA officials that it would continue its efforts to identify and control PCBs found at the Texas Eastern sites which may have been exposed to PCBs. (App. 350.) Texas Eastern also expressed a desire to reach an agreement on a remediation plan, possibly in the form of a consent decree, (App. 76), and criteria for determining how clean the Texas Eastern sites would have to be after remediation was completed. (App. 350; App. 351.)

EPA officials, specifically Michael Wood, were clearly displeased with Texas Eastern's continued use of its earthen pits after 1981, the date Texas Eastern claims that it first learned its pipeline liquids were contaminated with PCBs. (App. 350; App. 353.) Texas Eastern explained that the logistics of replacing the earthen pits required a gradual

phaseout, and made it nearly impossible to cease all use of the pits at that time. EPA indicated to Texas Eastern that some of the latter's activities, specifically the closing of the pits at its St. Francisville, Union Church, and Clinton compressor stations, by solidifying the PCB liquids with fly ash, (TRSOF ¶ 353), were almost certainly violations of TSCA.

In light of these discussions with EPA, Texas Eastern requested that Weston enlarge its study to include 54 additional compressor station sites (54-site survey). (TRSOF ¶ 354.) During the course of the 54-site survey, Weston communicated some of its findings regarding on-site contamination to some of Texas Eastern's employees, although the specifics of these conversations are not known. (App. 3 at No. 411.) In December 1986, Texas Eastern received a preliminary report of the results of Weston's 54-site survey. (App. 3 at No. 432.) Texas Eastern's attorney admitted at oral argument that the survey gave Texas Eastern reason to believe that off-site contamination had indeed occurred. (Tr. of Hr'g on Mot. for Summ. J., January 13, 1992 at 93-94.) A copy of this initial report was forwarded to EPA in December 1986. (App. 3 at No. 437.) Texas Eastern presented the final results from Weston's 54-site survey to EPA in March 1987. (TRSOF ¶ 391.)

In July 1986, Texas Eastern's Risk Management Department (which included its Insurance Department) was aware of the PCB presence in or on soil located at Texas Eastern's compressor station sites. (Dep. of Stephen Mulliken, App. 261 at 284-87.) At this time, Texas Eastern's Insurance Department requested that Querbes & Nelson, Texas Eastern's insurance brokers, compile a list of all CGL policies issued beginning in 1956. (Dep. of James Farley, App. 359 at 706.) The list was received by the

Insurance Department at the end of July or early August 1986. (*Id.*) Texas Eastern received information regarding claim notification requirements under these policies on or about December 9, 1986. (TRSOF ¶¶ 381, 383.)

On November 5, 1986, Texas Eastern representatives met with representatives from EPA and the Department of Justice to discuss PCB contamination at the compressor station sites. At the conclusion of the meeting, all parties understood that a judicially enforceable agreement would have to be entered into concerning the pit remediation. (TRSOF ¶ 368.)

9. *Texas Eastern's Problems Become Public Knowledge*

On February 21, 1987, several newspaper accounts of Texas Eastern's problems and its discussions with EPA were published. (TRSOF ¶ 387.) Prior to this time, Texas Eastern had not given notice to its insurers that it had entered into negotiations with EPA concerning the PCBs. (SOF ¶ 388.) During meetings held in London, England, in February 1987, concerning the renewal of Texas Eastern's liability insurance, Texas Eastern advised the London Underwriters that it had a PCB problem and that it was *not* making a claim against the insurers at the time "because the occurrences being investigated by Weston had not yet given rise to suits or claims against Texas Eastern," (App. 4 at 39. *See also* Dep. of David Fenton, App. 135 at 76-82), and because Texas Eastern believed that no third parties were involved. (Dep. of Stephen Mulliken, TApp. 2 at 304.) Texas Eastern discussed similar issues with representatives of its other lower-level liability carriers in March 1987. (App. 4 at 39.) On March 17, 1987, representatives of Texas Eastern testified before the United States Senate Subcommittee on Superfund and

Environmental Oversight concerning the PCB contamination of its earthen pits. (TRSOF ¶ 397; App. 2 at 2.)

10. *Texas Eastern's Negotiations with EPA*

On April 14, 1987, Texas Eastern met with EPA representatives for the purpose of outlining the framework within which a Consent Decree would be negotiated covering the cleanup of Texas Eastern's compressor station sites. (App. 381.) On August 18, 1987, in a letter to David Batson, EPA's chief negotiator, Carol Dinkins, Texas Eastern's attorney, outlined certain proposals made by Texas Eastern on which Ms. Dinkins believed an agreement had been reached. (App. 382.) By the middle of October 1987, both Texas Eastern and EPA came to an "Agreement in Principle" which the parties formally executed in writing in November 1987.

Ultimately, EPA and Texas Eastern entered into a consent decree in an action entitled *United States of America v. Texas Eastern Transmission Corp.* in June 1988. (TRSOF ¶ 411; App. 385.) The Complaint and the Consent Decree were both filed the same day. Pursuant to the Consent Decree, Texas Eastern was obligated to clean up property which it had contaminated with PCBs. All of the property was either owned or operated by Texas Eastern, and none of the property was owned by third parties. (TRSOF ¶ 499.) The Consent Decree required continued monitoring of groundwater under Texas Eastern's land, but did not specifically require or provide for remediation of any groundwater. Although Texas Eastern did not admit liability, it did agree to pay a civil penalty in the amount of $ 15 million. (App. 385 at 11.) Texas Eastern also agreed to reimburse EPA for costs already expended up to $ 1.5 million. The estimated total cost of the cleanup is presently in excess of $ 750 million.

Additionally, in April 1987, Texas Eastern entered into a Consent Decree with the Pennsylvania Department of Environmental Resources (PaDER) wherein Texas Eastern agreed to test soil and groundwater for possible PCB contamination and to remediate any discovered contamination. (Consent Order, App. 227C.) Subsequently, Texas Eastern also agreed to pay a penalty of $5.3 million to settle other PaDER claims that Texas Eastern had violated provisions of the Solid Waste Management Act, (35 Pa. Stat. Ann. § 6018.101 *et seq.*), and the Clean Streams Law, (35 Pa. Stat. Ann. § 691.1 *et seq.*).

Several other states initiated administrative or judicial actions against Texas Eastern alleging violations of state environmental laws, including New Jersey, Mississippi, and Kentucky. (*See* TE's First Am. Compl. ¶¶ 53-56, 65-68, 90-94; App. 227H-I; App. 227J-K; App. 227M-O.) The New Jersey action has been partially resolved, requiring Texas Eastern to pay a civil penalty in the amount of $850,000; however, issues concerning Texas Eastern's potential remediation responsibilities remain outstanding. The Mississippi and Kentucky actions have apparently been resolved by consent decrees.

Finally, as many as thirteen private third-party suits were filed against Texas Eastern alleging property and personal injury damage resulting from the PCB contamination. Only two of these complaints (the *Bondy* and *Atwood* actions) are actually involved in the present litigation, because I have denied Texas Eastern's motion for leave to amend its complaint and add the additional eleven complaints filed after the commencement of this action. (*See supra* pp. 10-11.) *Bondy v. Texas Eastern Transmission Corp.*, filed January 29, 1988, was terminated by summary judgment granted in favor of Texas Eastern.

(TE's First Am. Compl. at ¶ 104.) *Atwood v. Texas Eastern Transmission Corp.*, filed July 1, 1989, was terminated by a settlement between the parties.[31/]

11. *Texas Eastern's Notice to Its CGL Carriers*

Texas Eastern first gave formal notice of its negotiations with EPA, and of its "claim" under the various insurance policies, to its third-party liability carriers by letter dated August 19, 1987. (TRSOF ¶ 414.) After a December 9, 1987 meeting, in Houston, between Texas Eastern and the Carriers failed to resolve important questions concerning Texas Eastern's insurance claims, F & C filed suit against Texas Eastern, and as is recounted in the "Procedural History," this multidistrict litigation resulted. According to Texas Eastern, it has continued, at least up to January 1992, to provide the Carriers with copies of all relevant documents regarding the filing and settlement of claims arising out of the PCB contamination.

In sum, Texas Eastern now seeks a declaration that all of its costs incurred to comply with the EPA Consent Decree, the various state decrees and settlements, and the various private third-party actions are covered losses under the CGL insurance policies issued by the Carriers. The Carriers seek a declaration that they are not responsible for

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31/ The violations alleged in the state agency actions are in many respects duplicative of Texas Eastern's remediation responsibilities under the EPA Consent Decree. I have, therefore, focused primarily on the Federal Consent Decree in resolving these summary judgment motions. As I observed in my memorandum denying Texas Eastern's motion for leave to amend its pleadings, the private third-party actions raise factual issues which in some cases vary significantly from those presently involved in this case.

these costs. With the undisputed facts in mind, I will now address the issues, which in my view, are at the heart of this insurance coverage dispute.

IX. OCCURRENCE

The Carriers have moved for summary judgment on the issue of whether the PCB contamination constitutes an "occurrence" under any or all of Texas Eastern's insurance policies. The Carriers contend that Texas Eastern knew or should have known that it was polluting its own property and the property of third parties. Therefore, they argue, there was no "occurrence" pursuant to any of Texas Eastern's insurance policies because Texas Eastern "intentionally" caused all of the damage for which it is now seeking insurance coverage. Texas Eastern denies this allegation, and responds that since material factual disputes exist as to what Texas Eastern and its employees knew and intended, summary judgment is inappropriate on this issue. For the following reasons, I agree that factual disputes exist which prevent the granting of summary judgment on the "Occurrence" issue.

A. *The Policy Language*

The policies issued to Texas Eastern obligate the Carriers, in some cases, to indemnify the insured for, and in others, to pay on behalf of the insured

> sums which the insured becomes legally obligated to pay as damages because of bodily injury, personal injury or damage to or destruction of property caused by an *occurrence*.

(Ins.' Mot. Summ. J.—No Occurrence at 2) (emphasis original). The definition of an "occurrence" varies among the policies, but the Carriers admit that all of the policies provide coverage for an "accident," and none of the policies provide coverage for intentionally caused harmful acts.

B. *Texas Law*

It is a fundamental principle of insurance law that insurance contracts should provide coverage only when a loss is fortuitous. R.E. Keeton & A.I. Widiss, *Insurance Law* § 5.3 (a), at 475 (1988). The principle of fortuity is typically reflected in a liability policy's requirement that the insured's loss arise from an "occurrence" or an "accident." *Republic Nat'l Life Ins. Co. v. Heyward*, 536 S.W.2d 549 (Tex. 1976) and *Argonaut Southwest Ins. Co. v. Maupin*, 500 S.W.2d 633 (Tex. 1973) establish that Texas law is in accord with these general principles of insurance law. Under Texas law, harm which is the "natural and probable result" of intentional acts is not fortuitous and therefore is not covered by general liability insurance policies.

In *Maupin*, the insured removed some "borrow material" (sand and gravel) from the property of a third party under the mistaken belief that he had the property owners' permission to do so. The property's true owners subsequently sued the insured for trespassing on the property. The insurance carrier refused to defend the insured in the suit, contending that no covered occurrence had taken place because the suit alleged an intentional act

(trespass) and the policies only provided coverage for "accidents" or "occurrences." [32]

The *Maupin* court concluded that the removal of the sand and gravel was neither an accident nor an occurrence because the damage to the property was the "natural result" of the insured's intentional acts: "'Where acts are voluntary and intentional and the injury is the natural result of the act, the result was not caused by accident even though that result may have been unexpected, unforeseen and unintended.'" *Maupin*, 500 S.W.2d at 635 (quoting *Thomason v. United States Fidelity & Guar. Co.*, 248 F.2d 417, 419 (5th Cir. 1957)). That the insured was unaware of the property's true owners had no bearing on whether the trespass was caused by "accident." The insured did what he intended to do when he removed the sand and gravel from the property. The only mistake (or accident) made by the insured concerned the property's true ownership and the court concluded that the insurance policies did not provide coverage for accidents of that type. *Maupin*, 500 S.W.2d at 635.

In *Heyward*, the Texas Supreme Court again addressed the meaning of "accident," this time in the context of an accidental death rider to a life insurance policy. The court held that

> injuries are "accidental" and within the coverage of an insurance policy . . . if, from the viewpoint of the insured, the

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[32] The policy defined "occurrence" as "either (a) an accident, or (b) in the absence of an accident, a condition for which the insured is responsible which during the policy period causes physical injury to or destruction of property which was not intended." *Maupin*, 500 S.W.2d at 634 n.1.

> injuries are not the natural and probable consequences of the action or occurrence which produced the injury; or in other words, if the injury could not reasonably be anticipated by [sic] insured, or would not ordinarily follow from the action or occurrence which caused the injury.

Heyward, 536 S.W.2d at 557. It is settled Texas law that injuries which are the "natural and probable consequences" of intentional acts are not fortuitous injuries covered by insurance.

Numerous lower Texas courts are in agreement. For example, in *Baldwin v. Aetna Casualty & Sur. Co.*, 750 S.W.2d 919 (Tex. Ct. App. 1988) (writ denied), the insured allegedly damaged state roads by intentionally causing its admittedly overweight trucks to be driven on Texas highways. Citing *Maupin*, the court held that there was no accidental occurrence under the insurance policies because the act of continually sending out the overweight trucks was intentional, although the insured did not necessarily intend to damage the road. *Baldwin*, 750 S.W.2d at 921.

In *Southern Farm Bureau Casualty Ins. Co. v. Brock*, 659 S.W.2d 165 (Tex. Ct. App. 1983) (writ refused n.r.e.), the insured intentionally rammed his truck into a second vehicle to prevent the second vehicle's driver from shooting at someone. The court held that the insured was not entitled to recover for damage sustained by his vehicle under an automobile collision insurance policy covering only "accidental" damage. Citing both *Maupin* and *Heyward*, the court reasoned that the damage was not "accidental" because the insured "knew or should have known that the resulting damage to his vehicle was a natural

and probable consequence of his act." *Brock*, 659 S.W.2d at 166-67.

In addition to establishing the Texas courts' definition of "accident" and "occurrence," these cases clearly establish that Texas law determines an insured's intention "objectively" and not "subjectively." Texas courts have consistently framed the occurrence issue as "what the insured knew or *should have known*." *See, e.g., Brock*, 659 S.W.2d at 166-67; *Sanders v. Prudential Ins. Co.*, 697 S.W.2d 80, 81-82 (Tex. Ct. App. 1985) (interpreting *Heyward* to establish a "reasonable anticipation standard," and not a purely subjective one); *Chen v. Metropolitan Ins. & Annuity Co.*, 907 F.2d 566, 568 (5th Cir. 1990).[33/]

[33/] Though an objective test is used, it is not such a broad test as to deny coverage for any harm which is a reasonably foreseeable consequence of the insured's acts. Both Texas Eastern and the Carriers agree that, under Texas law, negligent acts are covered by third-party liability insurance policies. *See Massachusetts Bonding & Ins. Co. v. Orkin Exterminating Co.*, 416 S.W.2d 396, 400 (Tex. 1967). *In Kentucky Cent. Life Ins. Co. v. Fannin*, 575 S.W.2d 76 (Tex. Civ. App. 1978), Mrs. Fannin drove her car at a speed in excess of 100 miles per hour, lost control of the car, and was killed. The court concluded that a jury determination that the death was "accidental" was reasonable because

> there is nothing in the act of driving at an excessive rate of speed and failing to stop at a stop sign, though both be [sic] violations of the law, which *per se* is calculated to produce bodily injury or death to the driver. Under some circumstances, either excessive speed or a failure to stop may result in injury or death, but it cannot be logically said that death is the natural consequence of either act.

(continued...)

Texas Eastern contends that the objective test is merely a product of the judicial interpretation of specific language in the standard CGL insurance policy defining an occurrence as "an accident which results in bodily injury or property damage neither expected nor intended from the standpoint of the insured." It is Texas Eastern's position that courts have developed the objective test by interpreting the policy term "expected." *See, e.g., New Castle County v. Hartford Accident & Indem. Co.*, 685 F. Supp. 1321, 1331 (D. Del. 1988). Texas Eastern urges that because the individual policies at issue in this case do not include the terms "unexpected" or "unintended," the test which should be applied in this case is a subjective one, requiring the Carriers to prove that Texas Eastern subjectively intended to cause the harm for which the Carriers refuse to provide coverage.[34/]

[33/](...continued)
Fannin, 575 S.W.2d at 81. (emphasis original). "[A]lthough Mrs. Fannin may have been voluntarily exposing herself to some danger," her actions did not invalidate her accidental death benefits. *Id.* at 80.

In *Freeman v. Crown Life Ins. Co.*, 580 S.W.2d 897 (Tex. Civ. App. 1979) (writ. ref. n.r.e.), the court permitted the recovery of an accidental death benefit, even though the insured was killed while driving under the influence of alcohol, reasoning that "the ordinary person who is insured by an accident insurance policy would consider his death in an automobile collision accidental even though at the time of the collision he may be intoxicated or otherwise negligent." *Freeman*, 580 S.W.2d at 901.

Clearly, then, under Texas law, coverage is precluded only when the harm was intended, or when the harm was a natural and probable consequence of an intentional act.

[34/] Texas Eastern relies on *Dayton Indep. School Dist. v. National Gypsum Co.*, 682 F. Supp. 1403 (E.D. Tex. 1988), *rev'd on other grounds sub nom. W.R. Grace & Co. v. Continental Casualty Co.*, 896 F.2d 865 (5th Cir. 1990), for the proposition that Texas law would

(continued...)

Texas Eastern's contentions do not stand up under scrutiny. Texas Eastern has not offered any Texas precedent which links the inquiry into the insured's intentions to any particular policy language. In my view, the Texas appellate courts have developed an objective test because it flows naturally from the language in *Heyward* directing a court to inquire whether the injury could "reasonably be anticipated by the insured." *Heyward*, 536 S.W.2d at 557. The objective test is additionally beneficial because it avoids the difficult task of determining the actual subjective intent of a party. Texas Eastern has not provided any compelling reason to depart from what I believe is settled Texas law and I conclude that Texas Eastern's intent should be determined objectively.[35/]

[34/](...continued)
require an insurer to establish that the insured acted either willfully, intentionally, or maliciously for the purpose of causing injury, in order to invalidate coverage on intentional conduct grounds. *Dayton*, 682 F. Supp. at 1408. In reaching the conclusion that Texas would apply a subjective test, the *Dayton* court relied on the Texas appellate court's decision in *Orkin Exterminating Co. v. Massachusetts Bonding & Ins. Co.*, 400 S.W.2d 20 (Tex. Civ. App. 1965), *rev'd on other grounds*, 416 S.W.2d 396 (Tex. 1967). Because I choose to rely on the more recent decisions of the Texas Supreme Court, *Maupin* and *Heyward*, I respectfully decline to follow the conclusion of the *Dayton* court.

[35/] Texas Eastern also challenges the applicability of the Texas precedent cited by the Carriers, contending that those cases were interpreting "accident" based policies while Texas Eastern's policies were "occurrence" based. Texas Eastern's arguments are without merit. First, Texas courts have concluded that "occurrence" based policies are substantially similar to the older "accident" based policies. *See, e.g., Maupin*, 500 S.W.2d at 634 (analyzing an "occurrence-based" policy under prior decisions based on "accident" policies and describing the two types of policies as similar). Second, Texas Eastern has admitted in
(continued...)

Under Texas law, there is no insurance coverage for harm which is the natural and probable consequence of an intentional act. The Carriers argue that the evidence of Texas Eastern's knowing and intentional pollution of its own property with pipeline liquids establishes undisputed material facts sufficient to grant summary judgment in their favor and against Texas Eastern on the issue of whether any covered "occurrence" happened.

C. *The Applicable Facts*

The application of the law to the undisputed facts would be a simple procedure if the parties agreed on the nature of the harm for which Texas Eastern actually seeks coverage. They do not. The Carriers contend that Texas Eastern is attempting to shift costs which it historically should have paid as normal operating expenses to properly store and dispose of its pipeline liquids. Texas Eastern characterizes the costs for which it seeks coverage as the result of the off-site migration of PCBs which Texas Eastern did not know were in the pipeline liquids and did not know had a tendency to migrate in soil or groundwater. The characterization of Texas Eastern's claim is therefore significant to, and in my view dispositive of, the "Occurrence" issue.

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[25](...continued)
its pleadings that the definition of "occurrence" is similar to the definition of "accident" in that both terms require the insured to suffer harm that is unintended. (*See* App. 4 at 30 (the variations in specific "occurrence" definitions contained in the policies are "irrelevant"); TE's Mot. Summ. J.—Trigger of Coverage at 4 n.4 ("The term 'accident' as used in [early accident based] policies is interpreted as the equivalent of 'occurrence.'").)

Texas Eastern's claim for coverage is predicated, at least in theory, solely on costs incurred to clean up actual damage to third-party property, and on costs incurred to prevent future damage to third-party property, caused by the past, present, and future migration of PCBs from Texas Eastern's property onto the property of third parties. Indeed, this is the only conceivable claim which would allow Texas Eastern to recover from its third-party liability carriers under any CGL policy. Both parties agree that Texas Eastern has no coverage under its third-party liability policies for damage to its own property which does not, at a minimum, create the possibility of future harm to third-party property. Therefore, for the purposes of this motion, I assume that Texas Eastern is making a claim only for cleanup costs related to actual or potential third-party harm.[36/]

To prevail on its motion for summary judgment as to there being no "occurrence," the Carriers must establish, with undisputed material facts, that Texas Eastern intentionally polluted third-party property or acted in a manner which would naturally and probably lead to the

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36/ It is worth noting that although I conclude that Texas Eastern has made a potentially cognizable claim for coverage, I have not, and will not, offer an opinion on the ultimate merit of the claim. It is, of course, another question whether Texas Eastern can prove that any of its cleanup costs are actually related to third-party harm and whether it can prove that any of the various policy exclusions would not invalidate its coverage. Although I can conceive of no way that Texas Eastern would be able to prove that a particular portion of its cleanup costs were specifically allocable to actual or potential third-party harm, that issue need not be presently decided. At present, Texas Eastern seems to contend that all of its cleanup costs are attributable to actual or potential third-party harm.

off-site migration of PCBs. Based on the present record, the Carriers have not met their burden of proof.[37/]

1. *Knowledge that the Lubricant Was Escaping into the Environment*

The Carriers have produced evidence which establishes that Texas Eastern knew that the seals on its compressor station casings were less than perfect. Specifically, Texas Eastern was allegedly aware, beginning in 1958, that seal oil lubricant was escaping the compressors and entering the compressor case where it was exposed to the natural gas in the pipeline.

As I have previously discussed, Texas Eastern also understood that the passage of some amount of lubricant into the compressor case was an inherent design of centrifugal compressors. Texas Eastern's own internal

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37/ The Carriers characterize this case as one where an intentional corporate polluter, motivated exclusively by financial gain, failed to properly handle and dispose of its industrial waste, and is now attempting to "dump" its problem into its insurance carriers' lap. In support of this contention, the Carriers have cited to record evidence tending to show that Texas Eastern was slow to act after it discovered the migration of pipeline liquids from its pits and the venting of lubricating oil out of its vent stacks. In addition, the Carriers have cited to evidence tending to show that senior management at Texas Eastern believed that its PCB problem was a regulatory one and not one for which its third-party liability carriers would provide any coverage.

The Carriers have not, however, established with undisputed facts that at the time Texas Eastern dumped the PCBs it knew or reasonably should have known that the PCBs would migrate onto the property of third-party landowners. Texas law does not require invalidation of coverage for third-party PCB contamination simply because Texas Eastern knowingly dumped pipeline liquids onto its property or knowingly dumped PCBs which it reasonably believed would not migrate off its own property.

documents establish that a large amount of lubricating oil was lost between 1958 and 1977. In the Carriers' view, the loss can only be adequately explained by oil escaping from the compressor and either traveling down the pipeline (and mingling with the other pipeline liquids, large amounts of which were later disposed of in open earthen pits) or being vented out of the compressor vent stacks with the natural gas during the start-up and shut-down of the compressors. Importantly, Texas Eastern does not deny that it was aware of the system's occasional failures, choosing instead to dispute only the extent to which senior management knew about the frequency and magnitude of the leaks.

In addition, the Carriers note, and Texas Eastern does not dispute, that Texas Eastern was concerned with the compatibility of the seal oil lubricant and epoxies used to coat the *inside* of the pipeline. The Carriers conclude that Texas Eastern must have known that at least some of the lubricant was getting into the pipeline. Texas Eastern has not adequately responded to this contention.

Texas Eastern does not present a significant amount of evidence to refute the Carriers' allegations. First, Texas Eastern argues that the compressor seal systems were supposed to be "closed systems" with no leakage or "consumption" of lubricant oil. It is clear, however, that numerous employees were working under the opposite assumption. More significantly, other than observing that it would be counterintuitive for a corporation to waste expensive seal oil, Texas Eastern has presented no evidence to establish that the "closed system" assumption was correct.

Second, Texas Eastern employee Walter Woods testified that significant seal oil consumption took place only during seal failure or malfunction. (Dep. of Walter Woods,

TApp. 18 at 295-96.) However, Woods also testified that he realized, no later than 1974, that the compressors did leak seal oil into the cases making them one of the prime consumers of lubricant oil. (Dep. of Walter Woods, App. 670 at 5-6.) Rather than supporting Texas Eastern's argument, Mr. Woods's testimony establishes that at least one member of Texas Eastern's senior management understood that the seal oil did not work perfectly and that a substantial amount of oil was lost to the compressor cases.

In addition, Texas Eastern continues to rely on the fact that its senior management was unaware of the extent of the seal oil failures which occurred, and the amount of oil which ultimately entered into the pipeline. If Texas Eastern's managers, responsible for running the individual compressor stations, knew that the lubricant oil was escaping down the pipeline, then Texas Eastern will be charged with that knowledge. As I previously stated, Texas Eastern will not be allowed to hide behind the fact that its senior management did not know some of the basic aspects of its compressor stations' daily operation.

Texas Eastern also contends that most of the lubricant was vaporized by the heat of the turbine engines much like oil in a car engine. Texas Eastern has not, however, offered any evidence to show that the heat of the turbines could possibly be responsible for such a large amount of consumption. [38/]

The Carriers contend that once the oil entered into the cases, there were only two paths which it could follow. It

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[38/] PCBs are, in fact, known to be highly heat resistant and difficult to remove. This is one of the reasons why cleanups are so expensive. The heat resistant quality was also one of the primary reasons they were used as a seal oil in the compressors.

could be blown out the vent stacks with the natural gas or it could be discharged down the pipeline with the natural gas. Texas Eastern does not seriously contest this fact.[29] In fact, one of Texas Eastern's employees, J.C. Elmore, wrote in a February 6, 1976 memorandum to Paul Hughen, that Texas Eastern did not actually get rid of its lubricant oil by using it in its compressor stations, but rather distributed the

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[29] Texas Eastern does offer one piece of evidence which it contends establishes that most of the seal oil lost to the compressor cases was typically recovered and reused. (App. 80.) This memorandum, dated August 5, 1976, from W.G. Marks to E.C. Riall, Jr., states that there were 3,900 gallons of leakage in the seal oil lubricant system, and that the leaked oil was "normally trapped, filtered and returned to the turbine reservoirs." (*Id.*)

At his deposition, however, A.B. Jarnagin testified that he compiled all of the information in the memorandum for Mr. Marks, including the figure representing the amount of oil leaked and recovered. In response to questions about what he meant when he wrote the term "leaks," Mr. Jarnagin explained that he was referring to leaks from "the inside of the equipment to the outside of the turbine, through metal joints," and not to leaks through the inner seal rings into the compressor cases. (App. 658 at 326-27.) In light of Mr. Jarnagin's testimony, the memorandum does not create a material dispute as to whether Texas Eastern knew that some oil escaping from the compressor into the compressor case was traveling either down the pipeline or out the vents.

oil throughout the pipeline.[40] (App. 211 at 010021973; Dep. of James Elmore, App. 697 at 166-69.)

Having entered the pipeline, the Carriers contend that Texas Eastern knew or should have known that the lubricant oil intermingled with other pipeline liquids. Texas Eastern responds that it was unaware of PCBs in the pipeline liquids until 1981. The evidence Texas Eastern provides to support this position is the deposition testimony of Texas Eastern employees claiming that they did not know, until 1981, that the oil was mixed in with the other pipeline liquids. (*See, e.g.*, Dep. of Earl Farmer, TApp. 25 at 233; Dep. of Dickran Tefankjian, TApp. 26 at 117-18; internal Texas Eastern memoranda, written after 1981, stating that Texas Eastern did not discover the pipeline liquid contamination until 1981, App. 286 at 1; App. 305 at 1; the Declaration of H. Douglas Church, TApp. 191 at ¶ 6; the testimony before a senate subcommittee of Howard Homeyer, President of Texas Eastern Gas Pipeline Co., that Texas Eastern was not informed of the pipeline liquid contamination until 1981, App. 2 at 17). This evidence does not refute the Carriers' evidence (SOF ¶¶ 43-47) that certain Texas Eastern managers *were* aware of the

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[40] Texas Eastern challenges the value of this evidence because J.C. Elmore was an employee in a staff position who had no responsibility for Texas Eastern's change-out program. I interpret this to suggest that perhaps this memorandum was not prepared in the "scope of Elmore's employment" and thus cannot be used to impute knowledge to Texas Eastern. Elmore's deposition clearly established, however, that he was involved in the change-out program and that the memorandum expressed his opinion of how the compressor stations worked. This does not suggest that it was necessarily Texas Eastern's corporate opinion that the lubricant oil was escaping down the pipeline or out the vents, only that one of its employees believed this to be the case.

contamination. [41/] Thus, Texas Eastern has not created a material dispute on the issue of whether Texas Eastern knew about the fate of the escaped lubricant oil.

Having established that the lubricant oil was knowingly intermingled with other pipeline liquids, the Carriers rely on Texas Eastern's admission that it discharged pipeline liquids into the unlined earthen pits from 1958 until 1984, and Texas Eastern's admission that the migration of PCBs began almost immediately after PCBs were placed in the pits, (*see* Hart Decl., Ex. 47 (Dep. of John Cherry); Ex. 48 at 215-18 (Dep. of Bradford Cushing)), to establish that Texas Eastern intentionally caused all of the harm for which it is now seeking insurance coverage. The Carriers also rely on the testimony of certain Texas Eastern employees who saw cloudy mists coming from the vent stacks indicating that liquid was being vented along with the natural gas, liquid which the Carriers contend was lubricant oil containing PCBs. (TSOF ¶ 120.)

Texas Eastern responds that it did not believe that the discharge of the liquids into the pits was considered a discharge into the environment. It offers evidence that from the viewpoint of its employees, the pits were considered containers which segregated the liquid from the rest of the environment, (TSOF ¶ 76), and destroyed the liquid either by burning, natural evaporation, or by carting the liquid away for permanent disposal. The Carriers challenge Texas Eastern's characterization of the pits as containers, and

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[41/] Texas Eastern cannot be heard to argue that because some of its employees were ignorant of the pipeline contamination that ignorance is imputed to the entire corporation. Since a sufficient number of Texas Eastern managers responsible for the daily operation of Texas Eastern's pipeline understood that lubricant oil was escaping into the pipeline, that knowledge will be imputed to the corporation.

contend that Texas Eastern understates its knowledge of the pits' shortcomings as containment vessels.

Concerning the viability of using the disposal pits as containment vessels, the Carriers point to significant amounts of evidence establishing that Texas Eastern was aware that the various compressor station sites had a history of discharging liquids from the pits, which occasionally made their way off-site. First, Texas Eastern's Effluent Discharge Survey indicates that only 8 of the 35 compressor station locations burned pipeline liquids in 1973. (App. 118; App. 119.) [42/] Thus, not all of the liquids were burned in the pits, as Texas Eastern has suggested. Next, the Carriers point to the same Effluent Discharge Survey to establish that some of the compressor stations reported that pipeline liquids were being absorbed into the ground, thus refuting Texas Eastern's contention that many of the pit sites had been backfilled and were therefore presumed to be safe containers, much like landfill sites. (*Id.*) Finally, the Carriers rely on evidence that over a twenty-five year period of time, Texas Eastern was presented with complaints from neighboring property owners alleging that pipeline liquids from the pits had overflowed onto their property. (SOF ¶¶ 114, 125, 130; Dep. of Roy Wolfe, App. 60 at 340; App. 137.)

Concerning the mists that were seen during the venting of natural gas from the compressor casings, Texas Eastern offers the testimony of a number of employees who claim that they believed the mist to be water or pipeline liquids and not any of the lubricating oil. (TSOF ¶ 120.) Texas

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[42/] These 8 stations were: Mt. Pleasant, TN; Owingsville, KY; Wind Ridge, PA; Holbrook, PA; Accident, MD; Marietta, PA; Perulack, PA; and Grantville, PA.

Eastern also relies on the Declaration of H. Douglas Church as evidence that Texas Eastern did not realize until 1987 that it had regularly vented lubricant oil (containing PCBs) in the regular course of business. (Church Decl., TApp. 191 at ¶ 8.) Finally, Texas Eastern contends that even if its employees knew that it was oil, the employees only saw the mist land on Texas Eastern's property and not on the property of third parties. (TSOF ¶ 120.)

Although it is Texas Eastern's position that it never intended to vent lubricant oil along with natural gas during start-up and shut-down of the compressors, various Texas Eastern employees testified that the venting included numerous instances of misty discharges. (TSOF ¶ 120; Dep. of Eugene Riall, App. 56 at 183-86; Dep. of Walter Woods, App. 670 at 812-14; Dep. of A.B. Jarnagin, App. 658 at 208-09.) Texas Eastern has not created a material dispute that it did not know that lubricant oil was vented along with the natural gas. It is still an issue of dispute, however, as to whether any of the vented oil reasonably should have been expected to migrate onto the property of third parties.

The Carriers respond that even if Texas Eastern is correct about the "containment" function of its pits and its lack of knowledge of the oil content of the mists, Texas Eastern does not adequately address the alternate ways in which the PCBs could and did reach the environment. The Carriers point out that there are drains in the basements of each of the compressor stations which directed leaked lubricant into the environment. (Dep. of Robert Salzer, App. 105 at 248-50.) Texas Eastern has not responded with any evidence to challenge this assertion, except the conclusory statement that Texas Eastern employees did not consider Texas Eastern property to be part of the "general" environment. Texas Eastern's argument is spurious. I

conclude, as a matter of law, that Texas Eastern's property is part of the "environment."[43/] Even if Texas Eastern's belief was reasonable at the time, it would not provide Texas Eastern with a valid defense because, under Texas law, its CGL policies would not provide insurance coverage for mistakes of this type. *See Maupin*, 500 S.W.2d at 635. All of this does not, however, establish that Texas Eastern understood that the PCBs were migrating off its property and onto third-party property.

After considering all of this evidence, I conclude that the Carriers have established, as a matter of law, that Texas Eastern was aware that liquids were escaping from the pits and contaminating the environment, which included both Texas Eastern's property and the property owned by third parties. This does not, however, conclusively establish that Texas Eastern understood that the pipeline liquids contained PCBs.

2. *Knowledge that the Lubricant Contained PCBs*

Texas Eastern contends that it was unaware that the seal oil lubricant used in its compressor stations contained PCBs until 1972, at which time Monsanto informed Texas

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[43/] Texas Eastern contends that the term "environment" had a different meaning during Texas Eastern's use of the pits as a containment facility. In Texas Eastern's view, pollutants entered the environment only "when they reached rivers and lakes—[but] not landfills." (TE's Mem. in Opp'n Summ. J.—No Occurrence at 14.) Texas Eastern's contention fails for two reasons. First, there is no evidence establishing that Texas Eastern believed all of the property which it owned or used at its compressor stations was not part of the environment. Second, Texas Eastern ignores the evidence that property damage was caused by overflow of the pits, as well as by venting and other sources.

Eastern of this fact. The Carriers have produced very little evidence to refute Texas Eastern's claim and certainly not enough to grant summary judgment on the ground that Texas Eastern knew prior to 1972 that PCBs were escaping from its own property and migrating onto third-party property.

The Carriers rely on the deposition testimony of Earl Farmer, a Texas Eastern employee, who testified that in 1958 he was aware that the composition of some lubricant manufactured by Monsanto, which he believed to be OS-81, was a "chlorinated polyphenyl in a phosphate ester mix." (Dep. of Earl Farmer, App. 19 at 90.) This testimony does not, however, conclusively establish that he knew that the oil Texas Eastern used contained PCBs, or even that any other Texas Eastern official knew or had reason to know that the lubricant manufactured by Monsanto, for use by Texas Eastern, contained PCBs.[44/]

The Carriers observe that Texas Eastern employee Walter Woods became aware between 1968 and 1972 that there was growing public concern over PCBs in the environment. Once again, this does not refute Texas Eastern's claim that it was not aware of the lubricant's PCB content until 1972. The Carriers also claim that there is some evidence that Walter Woods was looking to replace Turbinol-153 before Monsanto informed Texas Eastern of

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[44/] The Carriers also offer a June 28, 1968 memorandum from Texas Eastern's Superintendent of Design and Construction, W.M. Stephens, to Texas Eastern's Assistant Chief Engineer, R.E. Moore, indicating that MCS-153 "is formulated with chlorinated polyphenyl (Chlorinated aromatic hydrocarbon) and a phosphate ester." (App. 29 at 010037983.) Again, this evidence is insufficient for me to find, as a matter of law, that Texas Eastern was aware that its seal oil lubricant contained PCBs before 1972.

its decision to discontinue sales of the lubricant oil. The document which the Carriers rely on is a letter written by Woods dated January 7, 1972.[45] (App. 184.) In the Carriers' view, Woods recommended that Texas Eastern pursue the approval of a particular lubricant as a replacement for the Turbinol-153 because he was aware that Turbinol was a polychlorinated biphenyl based product. (*Id.*) Although this is some evidence from which a fact finder might infer that Texas Eastern knew about the PCBs in the oil earlier than the 1972 Monsanto decision to discontinue the sale of Turbinol-153, it does not conclusively establish that Texas Eastern knew about the PCBs, and it does not identify the specific time between 1958 and 1972 when Texas Eastern allegedly acquired this knowledge.[46]

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[45] This is the same date that Monsanto proposed that Texas Eastern sign a hold harmless agreement indemnifying Monsanto for any future liability arising out of the sale of Turbinol-153. *See supra* p. 39. Thus, one explanation for the memorandum is Woods's desire to quickly find a replacement oil, because Monsanto was making it difficult for Texas Eastern to continue to purchase Turbinol-153.

[46] The Carriers expend a considerable amount of effort attempting to document that Texas Eastern knew, prior to 1972, that the lubricant oil contained PCBs. Upon review of the evidence, it appears that the Carriers have established that Texas Eastern knew about the potential hazards of PCB use, but they have not shown that Texas Eastern was aware that the oil contained the PCBs.

In 1958, Monsanto did warn Texas Eastern that its workers should limit their exposure to the lubricant oil. (TRSOF ¶ 25; App. 47-49.) In the 1960s and 1970s, there was certainly a large amount of public attention regarding the potentially harmful effects of PCBs in the environment and the effects of PCBs in living creatures. In 1970, Monsanto began terminating the sale of PCB-based products and warned its customers not to allow the PCBs to become environmental pollutants. While all of this evidence supports the Carriers' contention

(continued...)

As a consequence of the Carriers' inability to establish that Texas Eastern knew that PCBs were in the lubricant prior to 1972, Texas Eastern's coverage cannot, at least as a matter of law, be invalidated before the January 7, 1972 date, on the basis that there was no "occurrence."[47]

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[46](...continued)
that Texas Eastern knew or should have known that PCBs were dangerous if discharged into the environment, it does not establish that Texas Eastern knew or should have known that PCBs were contained in its lubricating oil.

[47] It is tempting to grant summary judgment on the "Occurrence" issue with respect to damage caused after January 7, 1972. Though the issue is a close one, I will deny partial summary judgment here. The Carriers argue that since it was known that liquids from the pits were escaping to third-party property, as soon as Texas Eastern knew that the liquids contained PCBs, Texas Eastern must have known that PCBs were escaping to third-party property. This is not necessarily the case. Texas Eastern has suggested that it believed that the liquids which were escaping did *not* contain PCBs, even after it knew that PCBs were in the pipeline liquids dumped in the pits. That is, Texas Eastern believed that the PCBs remained entrenched in the pits, and that only non-PCB substances were entering third-party land. (*See, e.g.*, TApp. 200; Tr. of Hr'g on Mot. for Summ. J., January 13, 1992 at 90 (Texas Eastern did not know until 1987 that PCBs are "enveloped in the hydrocarbon, they don't adhere to the soil because the hydrocarbons pick the PCBs up and move them into groundwater and move them off of the site.")) Although I am personally inclined to agree with the Carriers that simple common sense should have alerted Texas Eastern to the possibility that PCBs were migrating with the lubricant either from the pits, the vent stacks, the drainage swales, or the spraying of the liquids on the fence lines dividing Texas Eastern's property from third-party property, and even though I have concluded in "Late Notice," *infra* p. 163, that Texas Eastern knew or should have known of off-site PCB migration at least by December 1986, the Carriers have not proved that, as a matter of law, Texas Eastern knew, in January 1972, that PCBs were migrating with the other pipeline liquids, and summary judgment regarding all harm occurring after January 7, 1972 will therefore be denied. Even if I

(continued...)

D. *The Alternative Theory of an Occurrence*

Recognizing the difficulty of their task, the Carriers have advanced an alternative theory: Texas Eastern intentionally released pipeline liquids into unlined earthen pits, thereby knowingly polluting the environment with hydrocarbons.[48/] Thus, even if Texas Eastern was unaware of the PCBs in the pipeline liquids, it knew that the liquids themselves were environmental pollutants if they migrated off Texas Eastern's property. In the Carriers' view, it is settled Texas law that once an insured intentionally causes harm of any kind (presumably this includes property damage to first or third-party property, personal injury, and bodily injury), all resulting damage is not covered by insurance, because the damage is not fortuitous, regardless of the ultimate scope and magnitude of the harm.

I do not read the Texas cases to require this result. In *National Life and Accident Ins. Co. v. Knapp*, 430 S.W.2d 84 (Tex. Civ. App. 1968) (writ refused n.r.e.), the court

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[47/](...continued)
did grant summary judgment on this issue, Texas Eastern would not be precluded from seeking coverage for damage caused prior to January 7, 1972, and Texas Eastern's experts have testified that the vast majority of PCB damage to third-party property occurred prior to 1972 due to the immediate migration of the lubricant oil downward into the subsurface of the pits. (*See* Hart Decl., Ex. 47 (Dep. of John Cherry); Ex. 48 (Dep. of Bradford Cushing); TApp. 203.)

[48/] Texas Eastern admits that in certain concentrations, hydrocarbons are damaging to the environment if they escape containment, which in the present case refers to an escape from the earthen pits. (TE's Mem. in Opp'n Summ. J.—No Occurrence at 16; Dep. of J. Clifton Williams, App. 117 at 235-36.)

decided that the intent to shoot an intruder in the leg, which ultimately resulted in the intruder's death, invalidated the shooter's insurance coverage because "[t]he insurer is not required to show that the actor had the specific intention to inflict the particular character of injury that flowed from the act." *Id.* at 90. In other words, the court found that the death of the intruder was an injury of a different magnitude than the result originally intended (mere injury), but was still sufficiently related to the intended harm as to be considered part of the natural and probable consequences of the original act.

In *Carpenter Plastering Co. v. Puritan Ins. Co.*, No. 3-87-2435-R, 1988 WL 156829 (N.D. Tex. August 23, 1988), the insured was aware of minor cracking and water damage due to defective asbestos wall panels, but the damage was later discovered to be much more extensive. The court reasoned that if the insured was aware of the problem, although unaware of the problem's full extent, it would be difficult to consider the accident "'unexpected.'" *Carpenter Plastering*, 1988 WL 156829, at *5. Once again the court was confronted with a situation where the ultimate harm was reasonably related to the expected harm.

These cases are considerably different from the situation alleged to have existed at Texas Eastern. This is not an example of damage which is merely more extensive or of a different magnitude. PCB damage is ordinarily of a completely different character and caused by a different instrumentality than hydrocarbon damage and is therefore unrelated to any hydrocarbon damage which Texas Eastern might have intentionally caused. Indeed, if Texas Eastern reasonably believed that PCBs did not migrate (although all parties agree that the PCBs did migrate), then it might be entitled to insurance coverage for at least some part of the

ultimate cleanup costs, absent some other reason to invalidate coverage.

I reach the same result on the Carriers' loss in progress argument. The loss in progress principle is intended to invalidate coverage for a loss which the insured understood was ongoing and for which it bought insurance coverage while only the extent of the loss was unknown. *See Carpenter Plastering*, 1988 WL 156829, at *5; *Appalachian Ins. Co v. Liberty Mut. Ins. Co.*, 676 F.2d 56, 63 (3d Cir. 1982); *Summers v. Harris*, 573 F.2d 869, 872 (5th Cir. 1978).

I have previously concluded that Texas Eastern knew that it was causing some property damage by releasing hydrocarbon liquids into the environment (including damage to third-party property) and that Texas Eastern knew it was releasing PCBs onto its own property. I have not concluded, however, that, as a matter of law, Texas Eastern knew or should have known that the natural and probable result of this activity was the release of PCBs onto third-party property.

If the loss for which Texas Eastern requested coverage was the damage to its own property, or even the damage to third-party property caused by the hydrocarbon liquids, the loss in progress principle would probably apply. However, since it is the damage caused by the PCB migration for which Texas Eastern seeks coverage, the loss in progress principle is inapplicable for the purposes of this motion.

The Carriers have failed to establish by undisputed facts of record that all of Texas Eastern's losses were not the result of an "occurrence" within the meaning of the CGL policies. Texas Eastern has likewise failed to establish by undisputed facts of record that any of its losses

were the result of an "occurrence" within the coverage of any of its CGL policies. For these reasons, the Carriers' motion for summary judgment on the "Occurrence" issue will be denied.

X. DAMAGES

Both parties have moved for summary judgment on the issue of whether Texas Eastern's losses are recoverable as "damages" under the specific language of its insurance policies. The Carriers contend that the costs of complying with the EPA Consent Decree and the various state decrees are not recoverable as "damages" which result from "property damage" or "bodily injury." Texas Eastern contends that these costs are recoverable.[49/] For the reasons that follow, I conclude that, under Texas law, the remediation costs and the EPA penalties are potentially recoverable as "damages," and the civil penalties paid to Pennsylvania and New Jersey are not.

The insurance policies issued to Texas Eastern by the Carriers generally provide coverage for "damages because of bodily injury or property damage." The Carriers contend that because the government claims sought only injunctive relief and not monetary compensation, the money expended by Texas Eastern to comply with the injunctions is not recoverable as "damages," which unambiguously refers to monetary relief. Alternatively, the Carriers contend that the government orders requiring expenditures by Texas Eastern are based not on existing or threatened property damage or bodily injury, but rather on regulatory violations, and are

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[49/] The parties agree that this issue does not affect the two private third-party claims which sought monetary damages from Texas Eastern.

therefore not recoverable as "damages" because of "property damage" or "bodily injury."

Texas Eastern responds that costs incurred to satisfy the injunctions are recoverable as "damages" because the term "damages," as it appears in the various insurance policies, is ambiguous and reasonably can be interpreted to include them. Additionally, Texas Eastern contends that the primary focus of the government actions was both actual and imminent property damage and a danger to the environment which would likely have caused bodily injury. As such, Texas Eastern claims that the costs are recoverable under its insurance policies.

A. *Equitable Relief as Damages*

The question of whether the costs incurred in complying with an injunctive order are "damages" is not a novel one. As with many of the issues raised in this litigation, numerous courts have reached different conclusions. Three circuit courts have reached the conclusion that these costs are not recoverable as "damages." *See, e.g., Continental Ins. Cos. v. Northeastern Pharmaceutical & Chem. Co. (NEPACCO)*, 842 F.2d 977, 987 (8th Cir.) (*en banc*), *cert. denied sub nom. Missouri v. Continental Ins. Cos.*, 488 U.S. 821 (1988) (Missouri law); *Maryland Casualty Co. v. Armco, Inc.*, 822 F.2d 1348, 1354 (4th Cir. 1987), *cert. denied*, 484 U.S. 1008 (1988) (Maryland law); *A. Johnson & Co., Inc. v. Aetna Casualty & Sur. Co.*, 933 F.2d 66, 69 (1st Cir. 1991) (Maine law).[50] However, at least four circuit courts have recently reached the opposite conclusion. *See,*

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[50] See also Grisham v. Commercial Union Ins. Co., 951 F.2d 872 (8th Cir. 1991) (reaffirming its decision in *NEPACCO*).

e.g., New Castle County v. Hartford Accident & Indem. Co., 933 F.2d 1162, 1190-91 (3d Cir. 1991) (Delaware law); *Independent Petrochemical Corp. v. Aetna Casualty & Sur. Co. (IPC)*, 944 F.2d 940, 947 (D.C. Cir. 1991), *cert. denied sub nom. Certain Underwriters at Lloyd's, London v. Independent Petrochemical Corp.*, 112 S. Ct. 1777 (1992) (Missouri law); *Aetna Casualty & Surety Co. v. Pintlar Corp.*, 948 F.2d 1507, 1513 (9th Cir. 1991) (Idaho law); *Avondale Indus., Inc. v. Travelers Indem. Co.*, 887 F.2d 1200, 1207 (2d Cir. 1989), *cert. denied*, 496 U.S. 906 (1990) (New York law).

The parties have found one Texas state court decision which addresses the question of whether, in the context of an insurance policy, an injunction can constitute "damages." *In Feed Store, Inc. v. Reliance Ins. Co.*, 774 S.W.2d 73 (Tex. Ct. App. 1989) (writ denied), the appellate court concluded that it could not. In *Feed Store*, the issue was whether an insurer was obligated to defend an insured against a trademark infringement suit which requested only prospective injunctive relief. The insurer had refused to defend on the ground that the CGL policy only obligated it to defend "any suit against the insured seeking damages," and the plaintiff in the underlying suit sought only injunctive relief.[51/]

[51/] The relevant portion of the policy read:

> The company will pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages because of personal injury or advertising injury to which the insurance applies . . . and the company shall have the right and duty to defend any suit against the insured seeking damages on account of such injury . . . .

Feed Store, 774 S.W.2d at 74. This language is substantially similar to language found in the insurance policies at issue.

The appellate court affirmed the lower court's judgment that the insurance company had no duty to defend against the suit. Specifically, the appellate court held that the underlying plaintiff's failure to seek "even one dollar in damages" was compelling, if not conclusive, evidence that the suit was for injunctive relief only, and not for damages. *Feed Store*, 774 S.W.2d at 74. The court reasoned that while the allegations underlying the suit could have supported a claim for damages, the controlling factor was what the complaint actually demanded. *Id.* at 75.

Although the opinion provides some guidance in predicting how the Texas Supreme Court would decide this issue, it is important to highlight the issues which the opinion did not consider. First, the court did not determine whether, under Texas law, the term "damages" was ambiguous or unambiguous. The *Feed Store* court explicitly stated that the parties agreed that the policy was unambiguous and, thus, the settled principle of Texas law requiring resolution of ambiguities in favor of the insured was "quite immaterial to [its] decision . . . ." *Feed Store*, 774 S.W.2d at 75. Second, the court was not faced with the question of whether an insurance company is obligated to defend and indemnify an insured in an action seeking injunctive relief which requires the insured to expend significant amounts of money in order to comply, as is the case in most environmental litigation. It is therefore helpful to review the decisions of other jurisdictions to predict how the Texas Supreme Court would decide the issue.

In *Armco*, an insurer brought a declaratory judgment action to determine whether it had an obligation to indemnify its insured for liability pursuant to the Comprehensive Environmental Response Compensation

Liability Act[52/] (CERCLA) for response costs and injunctive relief. Applying Maryland law, the Fourth Circuit reasoned that "'[d]amages,' as distinguished from claims for injunctive or restitutionary relief, includes 'only payments to third persons when those persons have a legal claim for damages.'" *Armco*, 822 F.2d at 1352 (quoting *Aetna Casualty & Sur. Co. v. Hanna*, 224 F.2d 499, 503 (5th Cir. 1955)). The court reasoned that this "somewhat narrow, technical definition of damages" was necessary because interpreting "damages" to include injunctive relief would render the term "mere surplusage, because any obligation to pay would be covered" by the contract. *Armco*, 822 F.2d at 1352. Because the suit against the insured sought injunctive relief, *Armco* concluded that the costs of compliance were not covered by the CGL policy.

In *NEPACCO*, the Eighth Circuit, sitting *en banc*, adopted a similar definition of "damages" under Missouri law and concluded that the insurer was not required to cover liability arising out of an EPA CERCLA action. The court conceded that "damages" may be an ambiguous term from the viewpoint of a lay insured, but concluded that the term is not ambiguous in the insurance context, and that the "plain meaning of the term 'damages'. . . refers to legal damages and does not include equitable monetary relief." *NEPACCO*, 842 F.2d at 985.

By contrast, the Third Circuit reached the opposite result in *New Castle County*, where the court reasoned that the question of whether cleanup costs incurred pursuant to CERCLA and the Resource Conservation and Recovery

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[52/] 42 U.S.C. § 9601 *et seq.*

Act[53] (RCRA) are "damages" is correctly answered by determining whether "damages" should receive a "legal, technical meaning" or a "plain, ordinary meaning." *New Castle County*, 933 F.2d at 1188. The court reviewed *Armco*, *NEPACCO*, and various other decisions holding that injunctive relief was not "damages" and concluded that those decisions rested on the courts' application of a "technical meaning" which excluded equitable relief from the definition of "damages." Delaware law required that the language in an insurance policy be given its plain, ordinary meaning and, if an ambiguity existed, it should be interpreted against the insurer. *New Castle County*, 933 F.2d at 1188-89. Thus, the court concluded that injunctive relief was insurable under the policies because "damages" could reasonably be interpreted to include such costs.

IPC reached a similar conclusion. In *IPC*, the Court of Appeals for the District of Columbia Circuit faced the identical issue decided by the Eighth Circuit in *NEPACCO*: Are response costs recoverable as "damages" under Missouri law? The court recognized that the Eighth Circuit was the "home" circuit for Missouri and was entitled to a degree of deference concerning the interpretation of Missouri law. Nevertheless, *IPC* concluded that under Missouri law cleanup costs were recoverable as "damages" under a liability insurance policy. *IPC*, 944 F.2d at 944-47.

The *IPC* court agreed with the *NEPACCO* court's conclusion that under Missouri law the language of an insurance policy is to be given the meaning that would ordinarily be understood by the lay person who bought and paid for the policy. *IPC*, 944 F.2d at 945. In the court's

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[53] 42 U.S.C. § 6901 *et seq.*

view, however, *NEPACCO* failed to apply this important principle of law, because it accepted a definition of "damages" used "'by astute insurance specialists or perspicacious counsel'" rather than one understood by the lay insured. *Id.* at 945 (citation omitted). *NEPACCO's* reliance on the "'legal, technical meaning,'" *Id.* (quoting *Armco*, 822 F.2d at 1352), violated Missouri's principles of interpretation and led the court to reach the wrong result. As in *New Castle County, IPC's* conclusion rests on its interpretation of the plain, ordinary meaning of the contract rather than on a purely technical definition of "damages."[54/]

Texas Eastern correctly observes that Texas law concerning the interpretation of terms in an insurance policy is analogous to Delaware law (and Missouri law). Texas courts do not permit policy terms to be confined to technical meanings unless they have been specifically so defined in the policy. *See Gonzalez v. Mission Am. Ins. Co.*, 795 S.W.2d 734, 736 (Tex. 1990); *United States Ins. Co. v. Boyer*, 269 S.W.2d 340, 341 (Tex. 1954) ("[T]he court in construing [an insurance] policy determines the everyday meaning of the words to the general public—the meaning of the words 'in common parlance'—'the usual and popular understanding of the term.'") (citations omitted); *Garrison*,

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54/ *See also Hazen Paper Co. v. United States Fidelity & Guar. Co.*, 555 N.E.2d 576, 583 (Mass. 1990) ("We explicitly reject the reasoning of some courts that incorporates '[p]revious judicial interpretations' into the insurance contract to narrow the scope of the word 'damages' and thus purport to eliminate any ambiguity. Lay people should not reasonably be expected to know such limitations.") (citations omitted).

765 S.W.2d at 538.[55/] As the Third Circuit recognized, resolution of the issue rests primarily on whether the term "damages" is ambiguous. The Carriers rely exclusively on *Feed Store* for the proposition that the Texas Supreme Court would conclude that, under Texas law, the term "damages" is unambiguous and refers only to monetary relief, and not to injunctive relief. *Feed Store*, however, did not consider the ambiguity question. I conclude that the Texas Supreme Court would not follow *Feed Store* and would instead conclude that the term "damages" is ambiguous and can reasonably be interpreted to cover costs incurred to satisfy the Federal and State Consent Decrees at issue in this case.

After reading *Feed Store*, I am not persuaded that the court was faced with the identical issue that is presented in this case. The complaint at issue in *Feed Store* clearly requested only traditional injunctive relief. The court reviewed the complaint and expressly found that the plaintiff had not alleged that it had suffered, or that it was seeking, monetary damages. Significantly, the opinion did not discuss whether the insured was obligated to take corrective action and whether such an expenditure would constitute "damages."

In my view, when a court issues an injunction, requiring a party to act or to refrain from acting, the average individual believes that any of the costs associated with compliance constitute "damages." The court in *NEPACCO* expressly recognized this fact. *See NEPACCO*,

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[55/] Texas law also instructs a court not to interpret an insurance policy term so as to render a portion of the contract meaningless. In my view, reading the policy to include coverage for an injunction of the type at issue here does not completely divest the term "damages" of meaning. More traditional injunctive relief may still be excluded from the definition of "damages" under CGL policies.

842 F.2d at 985. Because Texas law requires that insurance terms be given their plain, ordinary meaning from the standpoint of the insured, these costs, although incurred as a result of an injunctive order, should be recoverable.[56/]

An injunction issued pursuant to TSCA, RCRA or CERCLA is different in kind from injunctions issued in other contexts. Ordinarily, a court is not free to provide injunctive relief unless a party has established that it lacks an adequate remedy at law. An adequate legal remedy ordinarily takes the form of monetary damages, which would clearly be covered by insurance. In the environmental context, EPA is authorized to seek injunctive relief regardless of the adequacy of other legally sufficient remedies. These injunctions ordinarily require a party to incur large costs to remediate existing environmental damage. This power blurs the line between what might traditionally be considered damages (a remedy at law) and injunctive relief (a remedy in equity).

This distinction does not rely, however, on EPA's ability to choose between its various remedies. A number of courts have relied on the "fortuity" of EPA either (1) choosing to clean up environmental damage and sue the responsible parties for the costs expended by the government; or (2) choosing to sue the responsible party for a mandatory injunction to clean up the pollution in the first instance, to hold that costs expended to comply with injunctions are recoverable as "damages." *See, e.g., United States Aviex Co. v. Travelers Ins. Co.*, 336 N.W.2d

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56/ I agree with the Third Circuit that "the 'as damages' clause, read in its entirety, collectively conveys a single point—namely, that [an insurer] is obliged to indemnify [an insured] for money expended under the sanction of law to redress harm to property or persons." *New Castle County*, 933 F.2d at 1190 n.56.

838, 843 (Mich. Ct. App. 1983). Other courts have relied on the fortuity of EPA requiring a cleanup rather than suing for "environmental damages." While these reasons may add additional support for concluding that "damages" is broad enough to include Texas Eastern's response costs, in my view, the most relevant distinction is based on the injunction's ultimate effect on the insured.[57]

I therefore reject the Carriers' argument that because the EPA Consent Decree sounds primarily in TSCA and RCRA, as opposed to CERCLA,[58] Texas Eastern's cleanup costs are *per se* unrecoverable as "damages."[59] The Carriers believe that EPA's inability to remediate environmental harm and sue to recover the cost under TSCA and RCRA requires a different result regarding the insurability of an insured's costs of compliance with the injunction. In the Carriers' view, those courts holding that

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[57] I stated at the outset of this opinion that my sole task is to interpret the contracts that Texas Eastern and its insurance carriers entered into. In interpreting the term "damages," I believe that the actual effect of a requested remedy on an insured is particularly relevant to the issue of what an average individual would believe the term "damages" to mean. This is not identical to an inquiry into the "reasonable expectations of the insured," a doctrine of insurance contract interpretation not yet adopted in Texas. *See Mary Kay Cosmetics, Inc. v. North River Ins. Co.*, 739 S.W.2d 608, 613 (Tex. Ct. App. 1987).

[58] The parties vigorously dispute whether the EPA Complaint is best characterized as a "CERCLA remediation case" or a "TSCA/RCRA regulatory compliance case." In my view, the terms of the Complaint and the Consent Decree make it clear that EPA moved primarily under TSCA and RCRA to compel Texas Eastern to remediate its property, relying on CERCLA only to recover EPA's oversight costs.

[59] Of course, Texas Eastern must still establish that the damages are the result of property damage, bodily injury, or both.

CERCLA response costs are recoverable as "damages," rely on the fact that EPA might have decided to clean up the contamination and sue for damages, and refused to deny coverage because of the fortuity of EPA's choice. The Carriers conclude that under TSCA and RCRA, the fortuity risk is nonexistent, and that in this case, EPA could not have proceeded under CERCLA because it never made a finding that an "imminent and substantial danger to health and the environment" existed at the Texas Eastern sites.

These arguments are all beside the point, because I have not grounded my decision on mere fortuity. As the *Feed Store* court explained, the inquiry is not what might have been alleged but what was in fact alleged. No court should engage in a *post hoc* analysis of whether a party might have brought a particular action and I refuse to speculate about whether EPA might have brought an action against Texas Eastern based on grounds other than those stated in the EPA Complaint, or whether EPA might have proceeded under an entirely different statute.

In the present litigation, I am concerned with the issue of whether, under Texas law, the term "damages" is broad enough to include the costs incurred by Texas Eastern in complying with the EPA Consent Decree and various other decrees and settlements. I conclude that an insured's cost of complying with either a demand or an injunction to remediate property damage or bodily injury is the same whether issued under CERCLA, TSCA, or RCRA, and is therefore recoverable as "damages" under Texas Eastern's insurance policies.

B. *Compliance Costs as Property and/or Bodily Injury Damage*

The second issue raised by the parties is whether the costs incurred by Texas Eastern are losses due to "property damage" or "bodily injury." The Carriers contend that the EPA Complaint and the resulting Consent Decree merely seek to compel Texas Eastern to come into compliance with various environmental regulations and to remediate damage which has resulted from Texas Eastern's prior violation of those regulations. As such, the Carriers argue that Texas Eastern's costs are not recoverable because the costs of complying with federal and state regulations, and the costs of administering prophylactic measures to ensure future compliance, are not insurable.

Texas Eastern apparently concedes that the costs incurred merely to stay in compliance with regulations are not recoverable from the Carriers. Additionally, Texas Eastern must concede that any costs of remediating property damage which cannot be significantly linked to third-party harm are not recoverable because its CGL insurance policies only cover harm to third parties. It is Texas Eastern's view, however, that a large percentage of its costs were incurred primarily to remedy and prevent third-party property damage. Although I am doubtful of Texas Eastern's ability to ultimately establish this relationship, I conclude that a factual dispute exists on this issue requiring that both the Carriers' motion for summary judgment and Texas Eastern's motion for summary judgment be denied on this point.

Because factual disputes exist as to whether some of Texas Eastern's costs were or will be incurred to remediate third-party property damage and to prevent future harm to third-party property and third parties generally, I reject the

Carriers' contention that the mere fact that the majority of Texas Eastern's expenses were incurred pursuant to TSCA and RCRA establishes that the costs are not recoverable "damages." The Carriers have, however, raised serious issues concerning which of Texas Eastern's costs are potentially recoverable and which are not.

Texas Eastern cannot seek recovery of costs incurred solely to comply with federal or state environmental legislation. Even those courts which have allowed the recovery of CERCLA response costs under CGL policies have recognized that liability policies do not provide coverage for the costs of statutory and regulatory compliance. For example, in *Minnesota Mining & Mfg. Co. v. Travelers Indem. Co.*, 457 N.W.2d 175 (Minn. 1990), the Minnesota Supreme Court qualified its holding that CERCLA-imposed cleanup costs were recoverable by observing:

> We are not "opening the door," as the insurers assert, to insurance coverage of all business expenses which are mandated by the government . . . . These types of costs are not covered by the insurance policies simply because no property damage has occurred.

Id. at 184.

Indeed, Texas Eastern has admitted that it is not seeking coverage for those expenses which cannot be linked to property damage or bodily injury. Thus, the costs of complying with (1) TSCA regulations regarding the proper labeling of PCB containers; (2) TSCA regulations requiring the maintenance of adequate records of PCB storage and disposal activities; (3) RCRA regulations requiring

notification to EPA that Texas Eastern was managing hazardous waste; (4) RCRA regulations requiring Texas Eastern to obtain permits; and (5) RCRA regulations requiring Texas Eastern to comply with various record keeping and safety requirements are not recoverable.

Although I have previously concluded that the mere fact that EPA's Complaint was grounded on regulatory violations does not automatically preclude recovery of costs associated with compliance, it does make it more difficult for the insured to prove that its costs were incurred primarily because of property damage as opposed to mere regulatory violations. For example, the Carriers persuasively argue that many of the regulatory violations alleged in the EPA Complaint could have resulted in a mandatory injunction regardless of whether any property damage had in fact taken place. It would be Texas Eastern's responsibility to establish that each cost for which it seeks insurance coverage was incurred primarily because of property damage, bodily injury, or both. It would also be Texas Eastern's burden to establish that its costs were incurred not to implement prophylactic measures to prevent future regulatory violations, but only to prevent actual and imminent harm to third-party property.

In short, the fact that I have decided to deny summary judgment on this issue should not be viewed as a positive review of the merits of Texas Eastern's claims. It merely signals that Texas Eastern has offered sufficient evidence that would allow it to go forward and attempt to prove that at least some of its claims are recoverable, although it is my view that Texas Eastern would face a Herculean task in this regard.

C. *Civil Fines and Penalties*

One category of costs which Texas Eastern seeks to recover merits special attention: civil fines and penalties.[60/] To date, Texas Eastern has agre[illegible] to pay a $15 million penalty to EPA, a $5.3 million penalty to the PaDER, and an $850,000 penalty to the New Jersey Department of Environmental Protection (NJDEP) for violations arising under federal and state environmental laws. I conclude as a matter of law that the civil penalties assessed by PaDER and NJDEP are not recoverable as "damages"; however, the EPA penalty would be recoverable as damages under Texas Eastern's insurance policies.

1. *Choice of Law—Fines and Penalties*

Although the parties agree that Texas law applies to the majority of the issues in this litigation, the Carriers contend that the question of insurability of civil penalties should be determined pursuant to the law of the issuing jurisdiction. Therefore, the Carriers argue that the insurability of the EPA fine would be decided under the federal common law of insurance, and the insurability of the Pennsylvania and New Jersey fines would be decided under Pennsylvania and New Jersey substantive law, respectively. Texas Eastern responds that Texas law should be applied to decide the entire "Damages" issue and, pursuant to Texas law, civil penalties are insurable as "damages" to the

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[60/] The parties apparently believe that characterizing Texas Eastern's payments as civil "fines" (the Carriers) or as civil "penalties" (Texas Eastern) will effect the outcome of my decision concerning the payments' insurability. I do not share the parties' view. Because EPA, PaDER, and NJDEP characterize the payments as civil "penalties," I have used this designation throughout the opinion.

insured. In order to decide this issue, it is necessary to address the choice of law principles followed by both Texas and Pennsylvania.

The parties agree that I must apply the choice of law principles from the two forum states originally involved in this action: Texas and Pennsylvania. *See generally, In re San Juan Dupont Plaza Hotel Fire Litig.*, 745 F. Supp. 79, 81 (D.P.R. 1990); *In re Air Crash Disaster at Stapleton Int'l Airport*, 720 F. Supp. 1445, 1448 (D. Colo. 1988).[61/] In choice of law cases, Texas courts will apply "the law of the state with the most significant relationship to the particular substantive issue . . . ." *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414, 421 (Tex. 1984); *W.R. Grace & Co. v. Continental Casualty Co.*, 896 F.2d 865, 873 (5th Cir. 1990). The test is set forth in sections 6 and

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61/ In short, the parties contend, and I agree, that the claims in this case which were originally filed under diversity jurisdiction must be resolved under the laws of the forum state, including choice of law rules, in which they were originally filed: Texas and Pennsylvania. *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487, 496 (1941). The two circuit courts to decide the issue of whether courts whose jurisdiction is based on the FSIA would follow the laws of the forum state or use federal common law to determine choice of law questions are split. *Compare Barkanic v. General Admin. of Civil Aviation*, 923 F.2d 957, 959-61 (2d Cir. 1991) (the forum's choice of law rules apply) *with Liu v. Republic of China*, 892 F.2d 1419, 1425-26 (9th Cir.), *cert. dismissed*, 111 S. Ct. 27 (1990) (federal common law choice of law rules apply). Because this court is sitting in diversity on many of these claims, I choose to follow the Second Circuit's view that the forum's choice of law rules apply. To decide otherwise would require an almost impossible separation of the issues in this case.

188 of Restatement (Second) of Conflict of Laws.[62/]

[62/] Section 6 provides:

(1) A court, subject to constitutional restrictions, will follow a statutory directive of its own state on choice of law.

(2) When there is no such directive, the factors relevant to the choice of the applicable rule of law include

(a) the needs of the interstate and international systems,

(b) the relevant policies of the forum,

(c) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,

(d) the protection of justified expectations,

(e) the basic policies underlying the particular field of law,

(f) certainty, predictability and uniformity of result, and

(g) ease in the determination and application of the law to be applied.

Section 188 provides:

(1) The rights and duties of the parties with respect to an issue in contract are determined by the local law of the state which, with respect to that issue, has the most significant relationship to the transaction and the parties under the principles stated in § 6.

(2) In the absence of an effective choice of law by the parties (*see* § 187), the contacts to be taken into account in applying the principles of § 6 to determine the law applicable to an issue include:

(a) the place of contracting,

(b) the place of negotiation of the contract,

(c) the place of performance,

(d) the location of the subject matter of the contract, and

(e) the domicile, residence, nationality, place of incorporation and place of business of the parties.

These contacts are to be evaluated according to their relative importance with respect to the particular issue.

(3) If the place of negotiating the contract and the place of performance are in the same state, the local law of this

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Pennsylvania uses a modified version of the *Restatement (Second)* approach, which combines a relationship and interest analysis. *Compagnie des Bauxites de Guinee v. Argonaut-Midwest Ins. Co.*, 880 F.2d 685, 688 & n.9 (3d Cir. 1989) (citing *Griffith v. United Air Lines, Inc.*, 203 A.2d 796 (Pa. 1964)). This test "'takes into account both the grouping of contacts [listed in the Restatement (Second) of Conflict of Laws § 188(2) (1971)] with the various concerned jurisdictions and the interests and policies that may be validly asserted by each jurisdiction.'" Compagnie des Bauxites, 880 F.2d at 689 (quoting *Melville v. American Home Assurance Co.*, 584 F.2d 1306, 1311 (3d Cir. 1978)). *See also General Star Nat'l Ins. Co. v. Liberty Mut. Ins. Co.*, 960 F.2d 377, 379 (3d Cir. 1992) (citing *Cipolla v. Shaposka*, 267 A.2d 854, 856 (Pa. 1970) ("Pennsylvania rule requires examination of the significant contacts as they relate to the states' public policies underlying the issue in question.")

Since 1961, Texas Eastern's principal place of business has been Houston, Texas.[63] After moving its headquarters to Texas, Texas Eastern routinely sent its insurance applications and paid its insurance premiums from Houston. Additionally, Texas Eastern appears to have co-brokered the acquisition of its insurance policies through John L. Wortham & Son and Querbes & Nelson, Inc., headquartered in Houston and Shreveport respectively. Notice of the claims at issue in this case was made from Texas Eastern's headquarters in Houston.

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[62](...continued)

state will usually be applied, except as otherwise provided in §§ 189-199 and 203.

[63] In 1961, Texas Eastern moved its headquarters from Shreveport, Louisiana.

Republic Insurance Company, Highlands Insurance Company, and Ranger Insurance Company have their principal places of business in Texas. (Ins.' Mot. Summ. J.—Choice of Law at 10.) Although the other insurance carriers have their principal places of business elsewhere, the majority of them do business in the State of Texas. (TE's Mem. in Opp'n Summ. J.—Civil Penalties at 12 n.15.)

The environmental damage took place in as many as fourteen states including Texas, Pennsylvania, and New Jersey. Finally, to date, penalties have been imposed by EPA, PaDER and NJDEP.

The parties agree that on all other issues, no other state has a more significant contact to the present litigation than Texas, based largely on the fact that Texas Eastern is headquartered in Texas, environmental damage occurred in Texas, and many of the Carriers do business in Texas. The relevant question, therefore, is whether the nature of the civil penalties creates a significant relationship to the assessing state which overrides the Texas contacts.

The first step in the choice of law analysis is to determine whether the substantive laws of the states which have a possible interest in a particular issue would reach a different result. If the answer is yes, then I must determine whether the various choice of law analyses choose different substantive law. Again, if the answer is yes, I must choose between the competing choice of law analyses.

On the issue of civil penalties, the states which have a significant interest are Texas, Pennsylvania, and New

Jersey.[64] Only New Jersey has decided this issue, concluding that civil penalties are not insurable as a matter of public policy. *Township of Gloucester v. Maryland Casualty Co.*, 668 F. Supp. 394, 401-02 (D.N.J. 1987) (environmental fines and penalties are not viewed as "damages" and are thus uninsurable); *Blair v. Anik Liquors*, 510 A.2d 314, 318 (N.J. Super. Ct. Law Div. 1986) (indemnification for fines resulting from violation of Alcoholic Beverage Control laws violates public policy).

Neither Pennsylvania nor Texas has decided whether civil penalties are insurable. The best analogy provided by the parties is to the insurability of punitive damages. Under Pennsylvania law, punitive damage awards are not insurable because insurability would violate public policy. *Martin v.*

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[64] The Carriers have suggested that the insurability of penalties levied by EPA should be governed by the federal common law of insurance. I believe that the insurability of penalties assessed pursuant to federal environmental statutes should be governed by state law. As one district court recently concluded, "[w]hile environmental matters implicate broad national concerns, there is no authority for creating a federal common law of environmental insurance coverage . . . ." *A. Johnson & Co., Inc. v. Aetna Casualty & Sur. Co., Inc.*, 741 F. Supp. 298, 300 n.2 (D. Mass. 1990), *aff'd*, 933 F.2d 66 (1st Cir. 1991).

I also reject the Carriers' contention that federal environmental laws preempt the application of state law (if it would permit insurability of civil penalties) because "'such state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.'" (Ins.' Mot. Summ. J.—Civil Fines & Penalties at 10 n.6 (*quoting Hines v. Davidowitz*, 312 U.S. 52, 67 (1941) (footnote omitted)). The Carriers have made no showing that Congress expressly preempted state law or that an irreconcilable conflict exists between federal and state goals and, as such, the state law continues to apply. *See Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 255 (1984) (state law principles are not preempted by a federal regulatory scheme unless they are "expressly supplanted.")

Johns-Manville Corp., 494 A.2d 1088, 1096 (Pa. 1985). Under Texas law, punitive damages are insurable, at least for conduct which merely rises to the level of gross negligence. *American Home Assurance Co. v. Safway Steel Products Co.*, 743 S.W.2d 693, 704-05 (Tex. Ct. App. 1987) (writ denied). Therefore, a conflict appears to exist between the substantive law of the three states with potential interests in this issue.

Having found a conflict in the substantive law, I will apply the choice of law principles of Texas and Pennsylvania and determine whether they would select the same substantive law to be applied. Under Texas choice of law principles (following *Restatement (Second) of Conflict of Laws* § 6(1)), I must first look at Texas Insurance Code article 21.42 which states a preference for applying Texas law to an insurance contract involving a Texas citizen and an insurance company that does business in Texas. *See* Tex. Ins. Code Ann. art. 21.42. For the purposes of this discussion, I assume that Texas Eastern, by virtue of its headquarters in Houston, Texas, is a Texas citizen pursuant to article 21.42. As I have previously indicated, most of the insurance companies involved in this litigation do business in Texas. Thus, it would appear that Texas choice of law rules would apply Texas substantive law to this issue.

The Carriers correctly observe, however, that the statute's application is limited to situations where the article would not give extraterritorial effect to Texas law. *See generally, W.R. Grace & Co.*, 896 F.2d at 883. In my view, the Texas Supreme Court would conclude that relying on article 21.42 to apply Texas law to the issue of civil penalties imposed by other states, or to civil penalties imposed by EPA, would be constitutionally permissible, in light of the fact that this litigation involves a dispute

between a Texas insured and insurers who have significant contacts with Texas. Therefore, under Texas choice of law principles, Texas substantive law applies.

Under Pennsylvania's choice of law principles, I must balance the various state interests with the public policies underlying those interests. In my view, Texas's interest is making certain that Texas insureds receive all of the benefits for which they contract with insurance carriers. This includes insurance coverage for civil penalties. Pennsylvania's interest is its ability to effectively enforce Pennsylvania laws.

There is little doubt that limiting the insurability of civil penalties does affect Texas's policy concerns. It may well be that Texas Eastern believed it was contracting for coverage of civil penalties that it incurred as a result of operating its natural gas pipeline. However, from Pennsylvania's standpoint, the inability to enforce its laws by the assessment of civil penalties may well hamper its ability to force compliance without resorting to criminal or other more severe sanctions. It would appear that a state can hardly have a more significant contact with the issue of a fine's insurability than in a situation where a foreign corporation doing business within its borders violates its laws, damages its property and natural resources, and is therefore fined as a punishment for the violation, and as a future inducement to comply with the state's laws. Combined with a public policy against the indemnification of liability incurred as punishment, I conclude that under Pennsylvania's choice of law rules, Pennsylvania's substantive law applies. For the same reasons, New Jersey substantive law would apply to the insurability of the New Jersey fines.

Because the choice of law principles lead to divergent choices of substantive law, I must choose between the two. *See e.g., Dupont Plaza Hotel Fire*, 745 F. Supp. at 87-88. Although I have not found explicit guidance on this point, I will apply federal common law to determine whether to use Texas choice of law principles or Pennsylvania choice of law principles. Federal common law follows the *Restatement (Second) of Conflict of Laws*. *Schoenberg v. Exportadora de Sal. S.A. de C.V.*, 930 F.2d 777, 782 (9th Cir. 1991). Based on Pennsylvania's need to enforce its laws, I believe that Pennsylvania has the most significant contacts concerning the "Fines and Penalties" issue and I will therefore apply Pennsylvania choice of law principles.

2. *New Jersey Fines*

As previously explained, under Pennsylvania choice of law principles, the penalty paid to New Jersey would be governed by New Jersey substantive law. As such, they are not insurable, and Texas Eastern would not be entitled to recover these losses from its insurance carriers.

3. *Pennsylvania Fines*

Under Pennsylvania choice of law principles, the Pennsylvania penalties would be governed by Pennsylvania law. Relying on Pennsylvania's refusal to permit insurance against punitive damages, I conclude that Pennsylvania would likewise refuse to permit insurance against civil penalties assessed for the violation of Pennsylvania's environmental laws.

4. *EPA Fines*

Under Pennsylvania choice of law principles, the EPA penalty would be controlled by the substantive law of

Texas.[65/] No federal common law of insurance exists, and as between Texas and Pennsylvania, Texas has the most significant relationship to the insurability of penalties because of Texas Eastern's contacts with Texas, and because of the lack of any significant Pennsylvania public policy regarding the insurance of federally assessed civil penalties. Relying on Texas law which enforces insurance contracts for punitive damages, I conclude that Texas law would permit insurance against civil penalties.

One final issue remains concerning Texas Eastern's ability to recover civil penalties under Texas law. I have previously determined that the term "damages" can reasonably be interpreted to mean money expended under sanction of law to redress harm to property or persons. (*See supra* p. 91 note 56.) Although this definition does not necessarily mean that a reasonable person would conclude that penalties are covered as "damages," *see IPC*, 944 F.2d at 947, it is certainly reasonable that an ordinary person could. I conclude, therefore, that civil penalties can be recovered as "damages" under Texas law. However, as with all of Texas Eastern's claims, Texas Eastern would have the burden of establishing which, if any, of these penalties were imposed primarily to redress harm to third-party property before the Carriers would be obligated to reimburse Texas Eastern.

[65/] Since Texas choice of law principles would also apply Texas substantive law, it is technically unnecessary for me to decide between Texas and Pennsylvania choice of law principles on the EPA penalty issue.

XI. OWNED PROPERTY EXCLUSION

Both the Carriers and Texas Eastern have moved for summary judgment based on the owned property exclusion.[66] Although the precise wording of the owned property exclusion varies, the following provision is representative of the exclusion as it appears in many of the insurance policies:

> This policy does not apply
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> . . .
>
> to property damage to:
> (1) property owned or occupied by or rented to the Insured,
> (2) property used by the Insured, or
> (3) property in the care, custody or control of the Insured as to which the Insured is for any purpose exercising physical control; but parts 2 and 3 of this exclusion do not apply with respect to liability under a written sidetrack agreement and part 3 of this exclusion does not apply with respect to property damage (other than to elevators) arising out of the use of an elevator at premises owned by, rented to or controlled by the Named Insured . . . .

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[66] Not all of the policies contain owned property exclusions, and this section of the opinion only applies to those policies containing such exclusions. Additionally, the parties agree that the owned property exclusion does not apply to groundwater remediation in those states where the groundwater is not the property of the surface landowner. The parties apparently agree that, under present law, groundwater is the property of the surface landowner only in Texas, Indiana, and Mississippi.

Other policies simply exclude coverage for damage to property owned by the insured, or for loss of, or damage to, or destruction of, property owned by the named insured.

Texas Eastern argues that although the owned property exclusion precludes coverage for damage to its own property, the exclusion should not apply to the cost of remediation work on its own property that is aimed at preventing actual and continuing harm to third-party property, and anticipated future harm to third-party property.

Specifically, Texas Eastern contends that the majority of the remediation work in which it is engaged is aimed at stopping the migration of PCB contamination from Texas Eastern's property to third-party property through surface soil, subsurface soil, and groundwater migration. Texas Eastern relies on case law (from jurisdictions other than Texas) and the various consent orders and decrees into which it has entered to support its assertion.[67/]

The Carriers contend that the owned property exclusion is unambiguous, and in accordance with Texas

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[67/] Although Texas Eastern contends that the state orders, decrees, and settlements into which it has entered require Texas Eastern to remediate third-party property, the vast majority of Texas Eastern's cleanup obligations require Texas Eastern to remediate PCB contamination on Texas Eastern's own property. Any liability which Texas Eastern has incurred pursuant to state orders, decrees, or settlements makes up a very small percentage of Texas Eastern's total response costs, because Texas Eastern is obligated to perform similar remediation work under the EPA Consent Decree. Accordingly, I will treat Texas Eastern's liability pursuant to state actions together with the EPA Consent Decree for the purposes of deciding the "Owned Property Exclusion" issue.

law, must be given its plain, ordinary meaning. In the Carriers' view, any damage to property owned, rented, or controlled by Texas Eastern is not covered by any of the insurance policies which contain an owned property exclusion. In the alternative, the Carriers urge that Texas Eastern be required to prove that any costs for which it seeks insurance coverage were incurred to remediate actual third-party property damage or to prevent future third-party harm which is imminent, immediate, and substantial.

Neither Texas Eastern nor the Carriers have cited a Texas state court decision, or any decision applying Texas law, which has considered the applicability of an owned property exclusion to a situation analogous to the present litigation. However, Texas Eastern has cited numerous cases from other jurisdictions which have concluded that the owned property exclusion does not bar an insured's recovery for cleanup work on its own property when the focus of the cleanup was the prevention of third-party harm.

For example, in *New Castle County v. Continental Casualty Co.*, 725 F. Supp. 800 (D. Del. 1989), *aff'd in part and rev'd in part on other grounds, New Castle County v. Hartford Accident & Indem. Co.*, 933 F.2d 1162 (3d Cir. 1991), the district court refused to deny coverage for New Castle County's cleanup costs of the Tybouts Corner landfill on the basis of an owned property exclusion. The court noted that the primary focus of the three lawsuits against the County (one by EPA, and two by citizens living near the landfill site) was the release and continuing release of hazardous substances from the landfill to other properties and the surrounding drinking water. *New Castle County*, 725 F. Supp. at 816. On this basis, the court concluded that the property damage at issue was "off-site property damage" not owned, rented, or controlled by New Castle County. Because there was a continuing threat of off-site property

damage if the contamination on the insured's property was not remediated, the court held that the owned property exclusion did not bar coverage of the County's claims. *Id.*

In *United States v. Conservation Chem. Co.*, 653 F. Supp. 152 (W.D. Mo. 1986) the district court refused to exclude coverage based on an owned property exclusion for remediation costs incurred by the insured, Conservation Chemical Company (CCC), for cleaning up an industrial chemical waste disposal facility located on its own property. The costs were incurred pursuant to a complaint filed by EPA alleging that hazardous wastes which had been disposed of at the site were migrating from the site and posed a danger to public health and the environment. *Conservation Chem.*, 653 F. Supp. at 162.

The court concluded that "coverage of the abatement remedy on the CCC site designed to prevent damage or further damage to third parties cannot be denied on the basis of the owned property exclusion." *Conservation Chemical*, 653 F. Supp. at 200. The court noted, however, that this does not include elements of the CCC claim which relate to a remedy for damage confined to the CCC site itself. "To the extent that all or a portion of the remedy relates solely to damage to the CCC site itself and not to prevent off-site contamination, the 'Owned Property Exclusion' clearly applies, and such damage is not within the coverage provided." *Id.* The court left the determination of which costs were included and which were not for trial.

In *Consolidated Rail Corp. v. Certain Underwriters at Lloyds*, No. 84-2609, 1986 WL 6547 (E.D. Pa. June 5, 1986), *aff'd*, 853 F.2d 917 (3d Cir. 1988), a Consolidated Rail Corp. (Conrail) train derailed in Pennsylvania, spilling 32,000 gallons of chloroform onto the ground at and

surrounding the accident site. The chloroform liquid contaminated groundwater, storm sewers, and a nearby creek. While concluding that the governmentally mandated cleanup was clearly aimed at the prevention and mitigation of third-party harm, and thereby constituted "damages" as defined by Conrail's excess insurance policies, the district court permitted Conrail to recover its cleanup costs despite the fact that some of Conrail's expenditures were for cleanup of Conrail's own property, and Conrail's insurance policies explicitly excluded coverage for damage to property "owned by the named insured." *Consolidated Rail*, 1986 WL 6547, at *4-5.

In *Township of Gloucester v. Maryland Casualty Co.*, 668 F. Supp. 394 (D.N.J. 1987), the district court explained why it did not consider an owned property exclusion a bar to coverage of a cleanup which included property owned by the insured, Gloucester Township. The court reasoned that there was an ambiguity in the language of the exclusion concerning whether the exclusion precluded coverage of costs which were linked to both damage to third-party property and the repair of property owned by the insured. *Township of Gloucester*, 668 F. Supp. at 400. The court concluded that because ambiguities should be interpreted against the insurer, and because the cleanup costs were "inextricably linked" to the damage claims of a third-party, the owned property exclusion did not preclude coverage of those costs. *Id.*

Relying on these and other cases, Texas Eastern argues that the owned property exclusion in its insurance policies should not apply to the cleanup costs it has incurred, and will continue to incur, pursuant to the various formally concluded consent orders and agreements. Texas Eastern admits, however, that the Federal Consent Decree does not require it to remediate any off-site property. According to

the terms of the Decree, Texas Eastern must remediate surface soil contamination, off-site equipment areas (controlled by Texas Eastern), and monitor groundwater contamination levels (but not remediate any groundwater at this time). (App. 385; App. 227A at 95).

In light of these facts, Texas Eastern asserts that the focus of EPA's concern regarding the cleanup of Texas Eastern's property was the migration of PCBs from Texas Eastern's property to the property owned by third parties, and the potential future harm to said properties. The evidence which Texas Eastern proffers to support these assertions is sparse, but is sufficient to create a disputed issue of material fact as to whether Texas Eastern's cleanup costs were incurred *solely* because of damage to its own property, or whether some of Texas Eastern's costs are related to the prevention of third-party damage.

In support of its assertion, Texas Eastern has offered two affidavits sworn by Karen Hammerstrom, a scientist working in EPA's TSCA compliance section who helped prepare risk assessments for EPA regulations concerning healthy PCB levels in the environment, and who prepared risk assessments related to the EPA Complaint and Consent Decree. As previously explained, Texas Eastern offers these affidavits to establish that EPA considered the effects of PCB contamination on third-party property (off-site property) when it decided the level of cleanliness to which it would require Texas Eastern to remediate its property. (First Hammerstrom Affidavit, Hart Decl., Ex. 50 at attachment pp. 6-7; Second Hammerstrom Affidavit, Hart Decl., Ex. 50 at ¶¶ 3-5.) Specifically, Hammerstrom's risk assessment considers what level of *post*-remediation off-site PCB exposure would be acceptable to EPA. (Second Hammerstrom Affidavit, Hart Decl., Ex. 50 at ¶ 3.)

Additionally, Texas Eastern observes that EPA is charged with the protection of the environment and is by definition always concerned with potential third-party harm. In this regard, Texas Eastern offers the deposition testimony of one of its environmental experts, Bradford Cushing, who testified that due to PCB migration from Texas Eastern's property to third-party property and groundwater, unspecified off-site contamination has in fact occurred. (Dep. of Bradford Cushing, TApp. 223 at 435-36; App. 632 at Table 2.)

The Carriers respond, however, that any actual off-site pollution has not been specifically defined by any of Texas Eastern's experts and contend that if Texas Eastern wants to rely on off-site property damage to procure coverage, it must do so on a site-by-site basis, proving that a particular site has migrating PCBs, or is in immediate danger of migrating PCB contamination onto off-site property, before the Carriers are deemed liable for any of the cleanup costs. Texas Eastern responds that EPA did not require a site-specific cleanup program, choosing instead to require that all sites meet a particular PCB standard, without regard to what the PCB levels were at the time of the Consent Decree. Therefore, Texas Eastern does not know whether every site, or which individual sites, have migrating PCBs reaching third-party property.

The Carriers' primary contention is that the facts of the present case do not fit within the "judge made insurance law" on which Texas Eastern relies. The Carriers observe that the only *actual* damage that can be affected by Texas Eastern's cleaning up of its own property is on-site contamination. Thus, this case is distinguishable from the situation where EPA orders a polluter to remediate third-party harm which includes the cleanup of on-site property as one element of a greater third-party problem.

In this case, EPA limited its cleanup order to Texas Eastern's own property.

Having considered these arguments, I conclude that the Texas Supreme court would preclude coverage for Texas Eastern's costs which were not *primarily* aimed at preventing actual, as opposed to purely potential, harm to third-party property.[68] I further conclude that the evidence proffered by the Carriers is insufficient to mandate a finding that *none* of Texas Eastern's expenses incurred pursuant to the EPA Consent Decree, state government decrees, or private third-party actions were due primarily to prevent future third-party harm.[69]

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[68] In other words, Texas law would exclude all coverage if not one PCB had migrated off Texas Eastern's land, but would permit recovery for the cost of remediating actual third-party damage—including the cost of remediating PCBs on Texas Eastern's property—if the PCBs were imminently and substantially likely to migrate. If it were possible to precisely separate the cost of remediating third-party property from the cost of remediating imminently migrating PCBs, I would be inclined to limit Texas Eastern's recovery solely to actual harm. I have, however, made this one concession to practicality because of the near impossibility of absolutely separating the two types of costs.

[69] I reject the Carriers' contention that the owned property exclusion excludes coverage for the cleanup of any "damage" to the insured's own property. This interpretation of the exclusion necessarily precludes coverage for work done on the insured's property that is "damage" on the one hand, but is performed *primarily* to remediate actual harm to third-party property due to the migration of the same contaminants. Under the Carriers' view, even if Texas Eastern could establish that its response costs were incurred primarily to prevent third-party harm, the costs would not be covered by its liability insurance.

(continued...)

There is little doubt that the majority of courts to consider this issue have concluded that costs incurred to remediate damage on the insured's property in an attempt to prevent future damage to third-party property are not excluded under the owned property exclusion.[20] Having examined these decisions, I respectfully decline to fully adopt their rationale, and I do not believe that the Texas Supreme Court would choose to either.

In my view, the owned property exclusion is unambiguous. The clause clearly reads that damage to an insured's property is not covered under the CGL policy. This does not mean that all activity taking place on an insured's property is *per se* uninsured. If the activity is

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[69](...continued)

In my view, the definition of "occurrence" is broad enough to include environmental damage which has not harmed third parties, but is imminently, immediately, and substantially likely to do so. Thus, I also reject the Carriers' assertion that only actual third-party damage is recoverable by Texas Eastern under the terms of its liability insurance policies, because the policies' definition of an "occurrence" is not broad enough to cover future harm, regardless of the imminent, immediate, or substantial nature of that harm.

[20] *See, e.g., Allstate Ins. Co. v. Quinn Constr. Co.*, 713 F. Supp. 35, 40-41 (D. Mass. 1989), *vacated*, 784 F. Supp. 927 (D. Mass. 1990); *Unigard Mut. Ins. Co. v. McCarty's Inc.*, 756 F. Supp. 1366, 1369 (D. Idaho 1988); *Broadwell Realty Serv. Inc. v. Fidelity & Casualty Co.*, 528 A.2d 76, 82 (N.J. Super. App. Div. 1987); *Banker Trust Co. v. Hartford Accident & Indem. Co.*, 518 F. Supp. 371, 374, *vacated on other grounds*, 621 F. Supp. 685 (S.D.N.Y. 1981). *But see Wolf Bros. Oil Co. v. International Surplus Lines Ins. Co.*, 718 F. Supp. 839, 845 (W.D. Wash. 1989) (granting defendant insurance carrier's summary judgment motion on the ground that the remediation costs were either not covered under the policy or that they were excluded by the owned property exclusion because the cleanup occurred on the insured's property).

primarily undertaken to abate an existing risk of harm to a third party, then the owned property exclusion should not apply.

The rationale most often relied on by courts declining to enforce the owned property exclusion is that the failure to allow an insured to recover cleanup costs incurred prior to the actual occurrence of third-party damage creates an incentive for the insured to wait until third-party damage occurs before taking any preventive action. *See, e.g., Allstate Ins. Co.*, 713 F. Supp. at 40-41; *Broadwell Realty*, 528 A.2d at 81; *Consolidated Rail Corp.*, No. 84-26019, 1986 WL 6547, at *5. I find this rationale unpersuasive for three reasons. First, if the insured intentionally allows the damage to occur, no insurance coverage should be available because intentional damage is not insurable as an "occurrence" in a standard CGL policy. Second, even if insurance coverage was made available to pay for the cleanup of third-party property, it does not follow that insurance coverage would automatically become available for the damage to the insured's own property.[71/] Third, ample incentives exist to compel the insured to timely report and remediate contamination; the most significant being the potential for criminal sanctions in addition to civil penalties

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[71/] In my view, an insurer in Texas Eastern's position cannot hope to obtain insurance coverage for any more than the cost of cleaning up actual third-party property damage or that portion of harm to its own property which is primarily aimed at the prevention of imminent and substantial third-party harm. Therefore, the extra insurance coverage obtained by the insured provides a minimal incentive to allow the pollutant to migrate to third-party property.

for intentionally violating federal and state environmental statutes.[72]

An alternative explanation for allowing insurance coverage for potential third-party harm is that in environmental cases cleanup costs are often directly related to the length of time that the contaminant is left unremediated. *See, e.g., Allstate*, 713 F. Supp. at 40-41. Thus, an insurance company benefits by paying for the remediation before the pollutant migrates from the insured's property and onto the property of third-parties. *See Bankers Trust Co.*, 518 F. Supp. at 373.Under Texas law, insurance contracts are to be interpreted by the same rules of construction as any other contract. Thus, the terms are to be given their plain, ordinary meaning. It may be true that an insurance company would benefit from the early cleanup, and the parties are free to write a contract that provides for that type of coverage.[73] Texas Eastern and the Carriers entered into contracts which did not provide coverage for damage to the insured's property, and I refuse to alter the agreements which the parties freely made.

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[72] I also reject Texas Eastern's contention that notions of fairness, equity, or public policy require a different result. Although I agree that an insured who remediates unintended environmental harm before it contaminates other property has saved its CGL insurance carriers from liability for third-party harm, matters of financial fairness are better addressed in an action for restitution, grounded upon a claim of unjust enrichment, than by rewriting the parties' contracts.

[73] Texas Eastern might also have applied for Environmental Impairment Liability (EIL) Insurance which specifically provides coverage for environmental damage. There is some evidence which suggests that Texas Eastern considered such a purchase but later rejected the idea. (*See* App. 301.)

Finally, courts have relied on the fact that in the environmental context, the costs of cleanup and prevention of third-party and first-party damage are often inextricably linked, making it virtually impossible to equitably enforce the owned property exclusion. *See, e.g., Gloucester*, 668 F. Supp. at 400. While the task of separating the insurable costs may be difficult in some cases (I have previously indicated that it may be an impossible task in this case), I do not believe this difficulty is sufficient to invalidate the owned property exclusion. It is the insured's responsibility to present the insurer with claims that are covered by insurance. This responsibility includes the identification of costs which are recoverable and those which are not. The insured should not reap an additional benefit simply because damages are difficult to prove. If Texas Eastern cannot segregate its damages, then, under Texas law, it fails to satisfy a condition precedent to recovery under its insurance contracts, and the Carriers' obligation to indemnify will never mature.

Texas Eastern contends that no showing of any significant link between the third-party risk and the first-party remediation need be made before a court will allow recovery of the entire cleanup cost. To the contrary, many of the cases considering this issue, and on which Texas Eastern relies, have held that the threat of third-party damage must be significant before a court will allow the insured to recover the cleanup costs for damage to its own property. For example, a number of cases have limited their holding to situations where the danger is both imminent and substantial. In *Broadwell Realty*, the court summarized its holding: "We are thus convinced that abatement remedies designed to prevent imminent and immediate damage to third parties cannot be denied on the

basis of the owned-property exclusion." *Broadwell Realty*, 528 A.2d at 82.[24/]

Other courts have failed to expressly limit their holdings, but have reached their conclusions in situations where the danger to third-party property was clearly imminent, substantial, or both. *See, e.g., Allstate*, 713 F. Supp. at 41 (finding that the gas leak from the insured's property constituted a "demonstrated danger" to third-party property); *Conservation Chem.*, 653 F. Supp. at 175 (finding that the release of the hazardous substances constituted an "'imminent and substantial endangerment to the public or welfare of the environment'"); *Consolidated Rail*, 1986 WL 6547 (32,000 gallons of chloroform was spilled on the insured's property and the property of third parties, clearly creating a substantial danger of third-party harm).

Further, many of these courts explicitly recognized that the insured does not automatically receive coverage for all of its remediation costs. As one court explained, "[t]o the extent that all or a portion of the response expenses pertain solely to damage to the [insured's property] and not to prevent off-site contamination, the owned property exclusion clearly applies, and such damage is not within the coverage provided." *Broadwell Realty*, 528 A.2d at 82. *See also Conservation Chem.*, 653 F. Supp. at 200.

Although I agree with Texas Eastern that no consensus exists regarding the precise showing that an

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[24/] *See also Summit Assocs., Inc. v. Liberty Mut. Fire Ins. Co.*, 550 A.2d 1235, 1240 (N.J. Super. Ct. App. Div. 1988) (requiring the trial court, on remand, to determine whether the threat to third-party property was "immediate and imminent or whether it was an 'undefined and speculative future loss' which should be excluded from coverage.")

insured must make in order to secure coverage for costs incurred on its own property, my reading of the cases leads me to conclude that the insured must at a minimum establish that the costs of cleaning up its own property are significantly related to the cleanup of actual third-party harm or the prevention of future imminent and substantial third-party damage.

In the present case, Texas Eastern relies almost exclusively on the affidavits of Karen Hammerstrom to support its contention that the damages it suffered because of the EPA Consent Decree were the result of EPA's concern for potential off-site third-party harm. This evidence is sufficient to support the contention that the damage on Texas Eastern's own property is related to third-party harm for the purposes of deciding the present motions. Therefore, the Carriers' motion for summary judgment will be denied on the "Owned Property Exclusion" issue. I want to make it clear, however, that if this issue ever came to trial, Texas Eastern would have to establish that each dollar for which it seeks insurance coverage is substantially related to third-party harm.[75/]

[75/] I have explained on two other occasions that I doubt Texas Eastern will be able to make such a showing. Making Texas Eastern's burden even more difficult is evidence establishing that Texas Eastern believed that off-site migration was not an imminent or substantial danger. For example, Bradford Cushing testified at his deposition that EPA made a determination that "the [PCB] sites did not present an eminent [sic] and substantial endangerment requiring immediate action." (Dep. of Bradford Cushing, App. 304 at 446-47.) Likewise, Carol Dinkins testified that Texas Eastern represented to EPA that the PCBs did not represent a substantial endangerment. (Dep. of Carol Dinkins, App. 275 at 159-60.) It is clear to me that EPA would have ordered Texas Eastern to remediate the PCBs on its property whether or not the PCBs posed an immediate threat to third parties or the environment.

(continued...)

XII. POLLUTION EXCLUSION

Both the Carriers and Texas Eastern have moved for summary judgment on the issue of the applicability of two types of pollution exclusion clauses contained in a number of Texas Eastern's insurance policies. Texas Eastern seeks a ruling that pollution caused over a "period of years" can still have been "sudden and accidental" as required by the language of both pollution exclusions. The Carriers contend that pollution caused by intentional discharges over a period of years cannot be considered either "sudden" or "accidental" and that the undisputed facts conclusively establish that Texas Eastern's PCB discharges occurred over a period of almost thirty years, thus precluding any insurance coverage for Texas Eastern's remediation costs. For the following reasons, I agree with the Carriers and will therefore grant summary judgment in favor of those Carriers whose insurance policies contain a pollution exclusion. Texas Eastern's motion will be denied.

Many, but not all, of the insurance policies contain a pollution exclusion. In the policies that do contain such an exclusion, the exclusion generally takes one of the following two forms:

> 1. This policy does not apply to—bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases,

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75/(...continued)
Evidencing this is the fact that EPA discussed the pit remediation with Texas Eastern long before EPA realized that off-site migration had occurred. While this would not necessarily preclude coverage for some of the claims, it is further evidence that third-party harm was not the primary focus of the EPA complaint and of the EPA Consent Decree.

> waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any watercourse or body of water; but this exclusion does not apply if such discharge, dispersal, release or escape is sudden and accidental.
>
> 2. This insurance does not cover any liability for—Personal Injury or Bodily Injury or loss of, damage to, or loss of use of property directly or indirectly caused by seepage, pollution or contamination, provided always that this paragraph . . . shall not apply to liability for Personal Injury or Bodily Injury or loss of or physical damage to or destruction of tangible property, or loss of use of such property damaged or destroyed where such seepage, pollution or contamination is caused by a sudden, unintended and unexpected happening during the period of this insurance.

I will refer to the first type of exclusion as an "ISO exclusion" and the second version as a "London Market exclusion."

Under the terms of the ISO exclusion, the discharge of a pollutant invalidates any insurance coverage for bodily injury or property damage[76/] resulting from the discharge.

[76/] Texas Eastern has additionally requested a ruling that the government and private third-party actions which underlie this litigation seek damages for "personal injury" as well as for property and bodily injury. Specifically, Texas Eastern alleges that the migration of PCBs onto the property of third parties can be considered personal injury under the provisions of its various insurance policies. Having considered Texas Eastern's arguments, I reject this interpretation of the insurance policies.

(continued...)

[76/](...continued)

Contemporaneous with this opinion, I have filed a memorandum and order denying Texas Eastern's motion for leave to file an amended complaint which includes new private third-party lawsuits filed against Texas Eastern arising out of the PCB contamination. This litigation is therefore primarily concerned with the government actions requiring Texas Eastern to remediate the PCB contamination and to pay certain civil penalties. The EPA Consent Decree is grounded primarily on RCRA and TSCA claims, although it clearly includes an element of a CERCLA claim. The state claims are based primarily on state environmental laws which are similar to the federal statutes.

It is Texas Eastern's position that the EPA claims are codifications of common law trespass and nuisance causes of action and are therefore covered under the personal injury provisions which provide coverage for "wrongful entry" and in some cases "other invasion[s] of the right of private occupancy." I have read EPA's Complaint and can identify no claim expressly based on either trespass or nuisance. I reject Texas Eastern's contention that because one of the many motivations behind the federal legislation was the codification of the common law causes of action, a RCRA or TSCA action is thereby transformed into one for either trespass or nuisance.

It may well be appropriate in some cases to look behind the express pleadings of a complaint to determine whether an insurance carrier must defend or indemnify an insured for a particular claim, but I do not believe that Texas law requires a court or an insurance company to examine the legislative history of a federal or state statute to determine whether a particular statutory claim can be recharacterized as a covered common law cause of action.

Concerning the state government actions, Texas Eastern has provided insufficient evidence to allow me to conclude that there is any allegation of damage for personal injury in the common law form of nuisance or trespass. To the extent that Texas Eastern sought rulings that the nature of the EPA or other state government claims includes personal injury, its motion will be denied. The two private third-party actions do allege personal injury and the ISO pollution exclusion does not apply to those causes of action. The London Market exclusion does apply to personal injury, *see supra* pp. 124-25, and coverage for the private third-party complaints is barred by any insurance policies containing a London Market type pollution exclusion.

The exclusion contains an exception which restores coverage in the event that the discharge is both "sudden and accidental." Under the terms of the London Market exclusion, no insurance coverage exists for bodily injury, personal injury, or property damage caused by pollution or other contamination. The exclusion restores coverage in the event that the damage is caused by a "sudden, unintended, or unexpected happening."

As should be clear from my discussion of the facts, I have concluded that all of the damage in this litigation was caused by Texas Eastern's long-term and continuous release of PCBs on its own property. There can be no material dispute that absent the applicability of the relevant exception, those insurance policies which contain either of the two pollution exclusions provide no coverage to Texas Eastern.

The Carriers contend that they have offered undisputed facts which establish that Texas Eastern intentionally discharged pipeline liquids contaminated with PCBs into unlined earthen pits, intentionally discharged pipeline liquids into the atmosphere during the start-up and shut-down of the compressor units, and intentionally discharged pipeline liquids onto weeds and dirt roads during a twenty-five year period beginning in 1958. The Carriers move for summary judgment on the ground that the two pollution exclusions bar coverage and Texas Eastern cannot offer evidence sufficient for a reasonable jury to conclude that its conduct comes within the exception to either the ISO or London Market exclusion.

Texas Eastern responds that its discharges can be characterized as "sudden and accidental," or as "sudden, unexpected, and unintended." In support of this contention Texas Eastern argues that the term "sudden" is ambiguous

and can be interpreted to have more than one meaning. One meaning is a temporal one, as in "quick" or "abrupt." The second meaning is one without regard to the timing of the event, as in "unexpected" or "unintended." If "sudden" means "unexpected," then the mere fact that Texas Eastern's discharges occurred over a long period of time is not relevant to the applicability of the ISO or London Market exclusions. Texas Eastern further contends that its various discharges can be characterized as "accidental," and therefore both "unexpected and unintended," and fall squarely within the exceptions to both exclusions.

Concerning the ISO exclusion, there are two principal questions which must be addressed: (1) should the focus of the pollution exclusion analysis be on the discharge of the pollutant into the environment or on the resulting environmental damage, and (2) must "sudden" have a temporal meaning akin to "quick" or "abrupt," or can it also have a non-temporal meaning?

On the first issue, courts have been virtually unanimous in concluding that the focus of the pollution exclusion inquiry is on the initial discharge of the pollutant into the environment. For example, the Third Circuit recently concluded that "the plain language of the 'sudden and accidental' exception focuses on the nature of the discharge, not on the resulting environmental damage." *New Castle County*, 933 F.2d at 1202 (Delaware law). *Accord, Liberty Mutual Ins. Co. v. Triangle Indus., Inc.*, 957 F.2d 1153, 1157 (4th Cir. 1992), *petition for cert. filed* June 1, 1992, (No. 91-1945) (New Jersey law); *Broderick Inv. Co. v. Hartford Accident & Indem. Co.*, 954 F.2d 601, 607 (10th Cir. 1992) (Colorado law); *Hartford Accident & Indem. Co. v. United States Fidelity & Guar. Co.*, No. 91-4057, 1992 WL 87828, at *6 (10th Cir. April 30, 1992) (Utah law).

In my view, reading the pollution exclusion to focus on the resulting environmental damage, rather than on the discharge of the pollutant, merely repeats the restriction of coverage created by the definition of an "occurrence": the policy provides insurance coverage only for unintentional damage. This interpretation is contrary to the long standing Texas principle that, wherever possible, meaning should be given to all clauses of an insurance policy. I conclude, therefore, that the Texas Supreme Court would require that the "discharge" of the PCBs, and not the resulting environmental damage, be both "sudden and accidental"[77] in order for Texas Eastern to avoid the bar of the ISO pollution exclusion.[78]

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[77] *See Ogden Corp. v. Travelers Indem. Co.*, 924 F.2d 39, 42 (2d Cir. 1991) (concluding that the terms of the pollution exclusion require that the discharge meet both the "sudden" and "accidental" provisions in order to satisfy the exception to the exclusion). Texas Eastern apparently admits at page six in its memorandum in opposition to the insurers' motion for summary judgment that the focus should be on the discharge and not on the damage which the discharge ultimately causes.

[78] Texas Eastern has raised the additional arguments that it is entitled to a trial on the issues of (1) whether PCBs constitute a "pollutant" as defined by the insurance policies, and (2) whether depositing pipeline liquids into pits and spraying liquids into the atmosphere constitutes a "discharge" as defined by the insurance policies.

It is undisputed that Texas Eastern intentionally deposited pipeline liquids containing PCBs into its unlined earthen pits. As a matter of law, I conclude that this act is a "discharge[s], dispersal[s], release[s] or escape[s]" as defined by the ISO exclusion. It is also undisputed that Texas Eastern released pipeline liquids into the atmosphere during the start-up and shut-down of the compressor units. I conclude that these acts were either "discharge[s], dispersal[s], release[s] or escape[s]" as defined by the ISO pollution exclusion. Finally, Texas Eastern's intentional spraying of pipeline liquids to kill weeds and to wet down

(continued...)

As I have previously explained, Texas Eastern bears the burden of establishing either that the occurrence does not come within an exclusion *or* that it can meet the requirements of the exception to the exclusion. The applicability of the exclusion has been established, and the only question to be decided is whether Texas Eastern's loss falls within the narrow exception to the exclusion.

Under the terms of the ISO exclusion, Texas Eastern must prove that the discharge of pipeline liquids (contaminated with PCBs) was both "sudden and accidental." Texas Eastern contends that "sudden" has more than one reasonable interpretation and, pursuant to Texas law, must be considered an ambiguous term. Under Texas law, if a term in an insurance contract has more than one reasonable meaning, it is ambiguous as a matter of law, and must be interpreted against the insurer and in favor of providing insurance coverage. Texas Eastern argues that

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[20](...continued)
dirt roads is clearly covered by the plain language of the exclusion. Likewise, these events clearly constitute "happenings" as required by the London Market type exclusion. Therefore no disputed issue exists for trial.

It is equally clear that PCBs are covered by the plain language of the ISO and London Market exclusions. It is beyond dispute that PCBs are a toxic chemical. As such, the release of PCBs into the environment satisfies the language of both exclusions. If Texas Eastern had discharged a small amount of PCBs into a contained area, there might be a dispute as to whether that release constituted either "pollution" or "contamination." However, the undisputed facts reveal that substantial amounts of PCBs were released into the unlined earthen pits, dispersed into the air, and sprayed onto the ground over a long period of years. Texas Eastern has offered no reasonable argument to support its contention that the release of PCBs into the environment did not constitute "pollution" or "contamination" and thus the language of the ISO and London Market exclusions is satisfied.

"sudden" can reasonably be interpreted to mean "unexpected" or "unintended," without any reference to the duration of the occurrence. Thus, an event can be "sudden" without necessarily starting or ending "quickly," and can occur over a long period of time.

Texas Eastern's interpretation has some support in the case law. Of the numerous courts in jurisdictions other than Texas that have considered this question, approximately one-half have concluded that "sudden" need not necessarily have a temporal meaning. *See New Castle County*, 933 F.2d at 1195 n.60 & n.61 (collecting cases). The fact that other courts have concluded that "sudden" is susceptible to more than one reasonable meaning is some evidence that "sudden" may be an ambiguous term, but does not automatically require a finding of ambiguity. *Hartford Accident & Indem. Co.*, 1992 WL 87828, at *4; *New Castle County*, 933 F.2d at 1196. Indeed, it is my view that the split in authority is not particularly relevant because my sole responsibility is to attempt to ascertain what the Supreme Court of Texas would conclude.

The dictionary definition of "sudden" lends further support to Texas Eastern's position. For example, *Black's Law Dictionary* 1284 (1979) defines "sudden" as "[h]appening without previous notice or with very brief notice; coming or occurring unexpectedly; unforeseen; unprepared for." At the same time, *Webster's II New Riverside University Dictionary* 1157 (1984) defines "sudden" as "[t]aking place without warning"; "hasty : abrupt"; "brought about in a short time"; or "very quickly and unexpectedly." Clearly the two definitions cannot easily be fully reconciled.

Courts disagree, however, on the significance of these conflicting dictionary definitions. For example, when faced

with a similar issue, the Michigan Supreme Court recently refused to give any weight to the conflicting dictionary definitions presented to it as evidence that "sudden" was an ambiguous term. The court explained that if courts reasoned that dictionary differences on the definition of "sudden" is evidence in and of itself that the term is ambiguous, "it would be virtually impossible to write a contract that was unambiguous." *Upjohn Co. v. New Hampshire Ins. Co.*, 476 N.W.2d 392, 398 n.8 (Mich. 1991).

I agree with those courts holding that dictionary definitions are not significantly helpful in determining whether a term has two reasonable definitions. It will often be the case that different people reading different dictionary definitions of the same word will reach different and unique interpretations of that word. That does not automatically mean that every definition is itself reasonable. In the present case, it is certainly reasonable for a person to conclude from reading dictionary definitions that "sudden" need not have a temporal meaning. In my view, however, it is nevertheless an unreasonable and unacceptable interpretation of the term.[79/] I will therefore accord the conflicting dictionary definitions little weight.[80/]

[79/] It is significant that Black's Law Dictionary has the unreasonable definition of the term. Black's relies on case law, not laymen's understanding, to form its definitions.

[80/] Although the Third Circuit found the dictionary definition of "sudden" persuasive evidence, it agreed that conflicting definitions did not require a finding of ambiguity: "[W]e agree . . . that the existence of more than one dictionary definition is not the *sine qua non* of ambiguity. If it were, few words would be unambiguous." *New Castle County*, 933 F.2d at 1193.

Finally, Texas Eastern relies on the drafting history of the pollution exclusion to support its contention that "sudden" can have a non-temporal meaning. (*See* Hart Decl., Exs. 19-31.) The Carriers have urged, in their motion to strike, that I not consider this evidence because Texas law forbids the consultation of extrinsic evidence in determining whether a contract term is ambiguous. I have reviewed Texas law on this issue and conclude that it is appropriate to consider the wording of a contract in light of surrounding circumstances. *See Sun Oil Co. (Del.) v. Madeley*, 626 S.W.2d 726, 731 (Tex. 1981):

> If, in the light of surrounding circumstances, the language of the contract appears to be capable of only a single meaning, the court can then confine itself to the writing. Consideration of the facts and circumstances surrounding the execution of a contract, however, is simply an aid in the construction of the contract's language.

Id. Having examined the drafting history of the pollution exclusion, I conclude that it is indeed evidence that some of the pollution exclusion drafters considered the meaning of "sudden" to be "unexpected and unintended." In fact, the Third Circuit concluded in *New Castle County* that similar drafting history implied that an interpretation of the term "sudden" which included a non-temporal meaning "is at least plausible, if not plainly correct." *New Castle County*, 933 F.2d at 1198.

More significantly from my perspective, however, is the lack of evidence linking this non-temporal meaning of "sudden" to the parties to these particular insurance

contracts. For example, there is no evidence that the parties ever discussed the meaning of the term "sudden" or referred to the original intent of the drafters at the time of contract. There is little credible evidence even tending to show that the Carriers or Texas Eastern were aware of the drafters' explanation of the ISO pollution exclusion at the time Texas Eastern and the Carriers entered into their contracts of insurance.

Given the tangential relationship of the drafting history to the actual contracts entered into by the Carriers and Texas Eastern, I do not believe that the drafting history is persuasive evidence of the "facts and circumstances surrounding the execution of [the insurance] contract[s]." *Sun Oil Co.*, 626 S.W.2d at 731 (emphasis added). I will therefore consider it as some, but not persuasive, evidence that "sudden" can reasonably mean "unexpected and unintended" without any temporal restriction.

The parties have cited only one case applying Texas law which specifically addresses the meaning of the term "sudden" in the context of a pollution exclusion. In *National Standard Ins. Co. v. Continental Ins. Co.*, No. CA-3-81-1015-D, slip op., (N.D. Tex. October 4, 1983), the district court held that under Texas law, discharges of pollutants over "a period of years" could not be considered "'sudden and accidental.'" *National Standard*, No. CA-3-81-1015-D, slip op. at 9.

National Standard involved a tort action for bodily injury caused by exposure to chemical carcinogens released into the atmosphere by the insured. In holding that the

pollution exclusion[81/] precluded coverage under the policies, the court explained:

> These claimants assert only that they were exposed to the chemicals through the atmosphere. Regardless of the legal theory used, each of the causes of action they allege would require proof that the defendants discharged the chemicals into the atmosphere. Moreover, they assert that the harmful conditions continued over a period of years, and thus there is no basis in the allegations for describing the chemical discharges as "sudden and accidental." Accordingly, the insurers whose policies otherwise place them on the risk for these claimants, but which policies contain the pollution exclusion, have no obligation to defend these suits.

National Standard, No. CA-3-81-1015-D, slip op. at 9. I interpret this case to support my conclusion that under Texas law, (1) the focus of the analysis under the pollution exclusion is the discharge of the pollutant into the environment, and (2) "sudden" has a temporal meaning akin to "quick" or "abrupt."

It is worth repeating what should already be clear: my principal responsibility is to predict what the Supreme Court of Texas would conclude about the meaning of the term "sudden." I have been provided with some guidance from the district court in *National Standard*. I have also given significant thought to the issue and conclude that, if faced

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81/ The pollution exclusion was the ISO type exclusion.

with this issue, the Texas Supreme Court would decide that "sudden" is unambiguous and cannot reasonably be divorced from "swiftness," "quickness," or all temporal significance.[82/]

I reach this decision keeping in mind the strong presumptions in Texas law that a court must not create an ambiguity in a contract when none exists and must give effect to each term in an insurance contract. Having considered all of the evidence, I believe that a definition of "sudden" which divorces it from the meaning of "swift" and "abrupt" is an unreasonable and tortured interpretation and not one which the Supreme Court of Texas is likely to adopt. Having already concluded that the damages for which Texas Eastern seeks coverage was not caused "quickly" or "abruptly" (because Texas Eastern discharged PCBs into the environment over a long period of years), I find that the ISO exclusion bars coverage for Texas Eastern's claims.

The London Market exclusion is also clearly unambiguous and therefore bars coverage. This exclusion bars coverage of any liability for property, bodily, or personal injury caused by seepage, pollution, or contamination, unless such seepage, pollution, or contamination is caused by a "sudden, unintended and unexpected happening." In the context of this exclusion, "sudden" clearly has a temporal meaning. To interpret "sudden" to mean that the discharge must only be

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82/ In this regard, it is useful to recall the Fifth Circuit's statement about a lawyer's ability to create ambiguity: "As necessity is the mother of invention, so is ambiguity the father of multiple reasonable constructions, and where lawyers are involved, one never lacks an eager parent of either gender." *Ideal Mut. Ins. Co.*, 783 F.2d at 1238.

"unintended and unexpected" would create an obvious redundancy in the policy.

Although my finding that the discharges were not "sudden" is sufficient to bar coverage under either exclusion, the discharges were also clearly not "accidental." To the contrary, the discharges were intentional and deliberate. Texas Eastern contends that the discharge of PCBs was "accidental" because Texas Eastern was, at least during the earlier years in question, unaware of the PCB content of its discharges and that it did not know it was discharging a pollutant. I believe that the Texas Supreme Court would rule that where, as here, the substance, regardless of its content, is discharged intentionally, lack of knowledge of the substance's pollutant content does not make the discharge "unintentional" or "accidental."

Texas Eastern also suggests that the relevant "discharge" occurred when the liquids migrated onto third-party property and that this was "accidental." It is the insured's initial discharge, however, not the resulting damage or pollution, that is the focus of the inquiry under the pollution exclusion clauses. In this case, the relevant discharge occurred when the PCBs, whether known or unknown, were released and emitted from Texas Eastern's compressors. Those discharges were neither "sudden" nor "accidental" within the plain meaning of the ISO and London Market pollution exclusion clauses.

For all of these reasons, the policies that contain an ISO or London Market pollution exclusion clause do not afford coverage to Texas Eastern, and as to those policies,

summary judgment will be granted to the respective Carriers.[83/]

XIII. LATE NOTICE

Both the Carriers and Texas Eastern have moved for summary judgment on the issue of "Late Notice." The Carriers contend that the August 19, 1987 notice provided by Texas Eastern violated a condition precedent to insurance coverage, thereby relieving the Carriers of the duty to defend or indemnify any of the claims against Texas Eastern. Additionally, the Carriers contend that Texas Eastern's late notice prejudiced their ability to adequately evaluate the nature of the claims. Texas Eastern denies that the notice was late and further denies that the Carriers have suffered any appreciable prejudice due to the timing of the notice. I conclude that Texas Eastern's notice was late as a matter of law, and that the Carriers were prejudiced by such late notice. Therefore, the Carriers' motion for summary judgment will be granted as to all claims, and Texas Eastern's motion will be denied.

A. *The Policy Terms*

All of the insurance policies issued to Texas Eastern contain a condition precedent requiring Texas Eastern to give notice to the Carriers of both an "occurrence" and of a "claim or suit." The insured's duty is typically to provide

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[83/] I note that with respect to one policy issued by Aegis, effective from March 1, 1975 to March 1, 1981, Texas Eastern contends that the pollution exclusion was deleted by endorsement for the entire effective period of the policy, while Aegis contends that the exclusion was deleted only from 1978 to 1981. Because I will grant summary judgment under all policies on the issue of late notice, I do not decide whether this policy contained a pollution exclusion from 1975 to 1978.

notice of an "occurrence as soon as practicable," and to forward every demand, notice, summons, or other process, with regard to a claim or suit, "immediately."

The excess policies typically require notice only of an "occurrence which appears likely to result in liability under" the excess policies themselves. In addition, some of the excess policies contain a provision which provides that the failure to give timely notice does not prejudice the insured's rights under the policy if the insured initially believed that the "occurrence" was unlikely to involve that policy.[84/]

Texas Eastern's primary insurance coverage was provided by the F & C policies. Under the policies in effect from July 1967 to January 1981, the duty to notify the insurer arises only after notice of the "occurrence has been received by the Insurance Department or executive officer of the Insured." In the F & C policy effective from January 1981 to April 1988, the duty to notify arises only after notice of the "occurrence has been received by the Insurance Department of Texas Eastern Corporation."

B. *Accrual of Texas Eastern's Obligation to Notify Its CGL Insurers*

The Carriers' allegations concerning the precise time when Texas Eastern's obligation to provide notice accrued are vague. The Carriers' motion cites numerous events,

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84/ Record evidence establishes that prior to April 1987, Texas Eastern's senior management understood that cleanup costs would likely exceed $100 million. Although Texas Eastern has not strenuously argued that the excess carriers were entitled to notice some time later than F & C, its knowledge of the probable cleanup costs would foreclose such an argument.

beginning in 1981, which arguably triggered Texas Eastern's notice obligations.[85/] As I have previously discussed, the most relevant events for determining the accrual date of Texas Eastern's notice obligation are those events which establish an awareness of off-site migration. Events involving on-site PCB contamination are also relevant because they establish that Texas Eastern was, or should have been, aware of the magnitude of its PCB problem and, thus, affect the determination of what a "reasonable time" for notice after the accrual of the obligation should be. I will briefly outline the relevant events.

1. *1981*

The first significant event of which the Carriers allege Texas Eastern should have provided notice was the 1981 discovery of PCBs in a residential gas meter in Long Island, New York. Although claims were made against Texas Eastern for contribution to the costs incurred by gas distribution companies for cleaning up the PCBs, Texas Eastern provided notice of the claims only to one excess liability carrier but not to its primary or other excess insurance carriers. Texas Eastern contends that the distribution companies' intentions to seek contribution for their costs were not considered "claims," (App. 267), and also that Texas Eastern is not now seeking coverage for any money paid to reimburse its customers' costs. In addition, Texas Eastern observes that it was only one of a number of natural gas suppliers to the Long Island site, and that it was

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[85/] In fact, the Carriers have contended that Texas Eastern knew, beginning in 1958, that it had a significant PCB -related problem, suggesting the possibility of a notification obligation many years prior to the actual date of notice.

never conclusively established that Texas Eastern was the sole source of the PCB contamination, thus rendering the validity of such claims doubtful.[86] (Dep. of Willard Young, TApp. 20 at 431-36.) Nevertheless, the Carriers plausibly argue that this was an "occurrence" likely to (and which in fact did) result in a claim by third parties.

2. *1982*

In August 1982, Texas Eastern entered into two Consent Agreements with EPA, obligating Texas Eastern, *inter alia*, to test the lubricating oil in its compressors for the presence of PCBs. (App. 289; App. 290.) Texas Eastern contends, not too convincingly, that it did not give notice to the Carriers because it did not believe that this was a claim as defined by its CGL insurance policies. The Carriers observe that many of these costs are similar, if not identical, to the remediation costs for which Texas Eastern is now seeking insurance coverage. Examples of the costs include the installation of source control equipment, testing of pipeline liquids, and disposal of the PCBs. In addition, Texas Eastern learned, in 1982, that an unlined earthen pit at its St. Francisville station was contaminated with PCBs and might require remediation. (TRSOF ¶¶ 291, 293). There is no evidence, however, that Texas Eastern then knew that any of the PCBs were migrating off its own property. The inherent danger (migration of any liquid from unlined earthen pits) is, however, so obvious, that prudence should have guided Texas Eastern to notify its numerous insurance carriers of potential claims in the future.

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[86] Doubtful claims, however, do not do away with an insured's duty to notify its insurer.

Indeed, it certainly could be argued that the known PCB contamination in Texas Eastern's pits, which Texas Eastern insists was unintended, was an event which, in light of federal statutes and EPA's probable requirement of remediation, was likely to result in a claim by EPA. Although Texas Eastern attempts to ground its obligation to notify entirely on the likelihood of a claim resulting from migration of PCBs onto third-party property, it is clear that the major cause and basis of Texas Eastern's present claims is cost associated with the EPA mandated cleanup of PCBs on Texas Eastern's own property. Thus, the CGL carriers certainly would have expected to be notified of this event as soon as practicable" if, as now, Texas Eastern seeks to recover these costs from its insurers.[87]

3. *1983*

Texas Eastern admits that it partially prepared a generic Environmental Impairment Liability (EIL) insurance application in which it listed PCBs in its compressor lubricant as a possible source of a future claim. (TSOF ¶¶ 92-94; App. 301 at 000602547). The application was never completed or actually submitted to any insurance company and Texas Eastern contends that its Insurance Department never reviewed the application. Of course, an event which

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[87] Texas Eastern cannot have it both ways. If I were to accept Texas Eastern's argument that the owned property exclusion does not apply to environmental harm of this type, then Texas Eastern would have to prove that notice was not late with respect to claims for cleaning up its own property. Since it knew of this so-called occurrence as early as 1982, the notice was late as a matter of law.

Conversely, if I accept Texas Eastern's argument that notice is only required when there is a likelihood of a claim by a third party based on PCB contamination, Texas Eastern is all but admitting that the owned property exclusion applies to virtually all of these claims.

is likely to give rise to a claim pursuant to an EIL policy is not necessarily synonymous with an event likely to give rise to a covered claim pursuant to a CGL insurance policy.[88] This does establish, however, that as early as 1983, Texas Eastern was aware of the potential for future claims.

4. *1984*

It is undisputed that EPA, in late November or early December 1984, (App. 306), issued a complaint against Texas Eastern's subsidiary gas pipeline company, Transwestern, which serviced areas not involved in this litigation. At that time, Texas Eastern was completing, or had completed, the sale of the Transwestern pipeline to Houston Natural Gas (HNG).[89] In April 1985, Transwestern entered into a Consent Agreement with EPA, requiring Transwestern to clean up PCB contamination found in its earthen pits. (App. 306.) Texas Eastern subsequently entered into an agreement with Transwestern to pay for a percentage of Transwestern's remediation costs to be incurred prior to December 31, 1987, up to an aggregate amount of $2 million. Texas Eastern contends that it did not consider this a "claim or occurrence" pursuant to its insurance policies, (TRSOF ¶ 309), and is not seeking insurance coverage for these costs in the present action.

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[88] However, "Texas Eastern's Insurance Department believed that Texas Eastern already enjoyed the equivalent of EIL coverage under its general liability policies." (TSOF ¶ 94.)

[89] As late as January 11, 1985, however, Texas Eastern continued to operate the Transwestern system during the change of ownership. (App. 286.)

5. 1985

In a January 10, 1985 phone conversation, EPA representative Mike Wood told J.C. Williams, Texas Eastern's Director of Technical Services, that the Transwestern system pit cleanup would require a settlement agreement which would include, among other things, "the method of cleanup, a time schedule (i.e. how soon), to what PCB concentration, etc." (App. 286 at 2.) Texas Eastern admits that Wood advised Texas Eastern that it should make assessments of potential contamination at other Transwestern system locations also using pits. (*Id.*) Texas Eastern contends that it did not report this to its insurance carriers because it did not consider the Transwestern system contamination, or the suggestion to investigate potential contamination at other sites, to be a claim against Texas Eastern. It seems clear, however, that Texas Eastern knew that there was a likelihood of claims by EPA and state environmental agencies concerning the cleanup of Texas Eastern's pits. It is at least arguable that these events were "occurrences" likely to give rise to a claim and therefore triggered an obligation to notify many of the Carriers "as soon as practicable."

In August 1985, EPA issued a Notice of Non-Compliance to Texas Eastern's Delmont station for violations of TSCA regulations concerning the marking, storage, disposal, and record-keeping of PCBs. (App. 317.) A copy of this letter was forwarded to Texas Eastern Vice President, H. Douglas Church. (*Id.*) In a subsequent meeting with EPA, Texas Eastern discussed its plans for the closing of its unlined earthen pits.

In November 1985, Texas Eastern hired Roy F. Weston, Inc. to determine the nature and extent of the PCB contamination around the pits, and to devise a remedial

plan. (App. 323.) Texas Eastern began to receive results of Weston's initial six-site survey, which began with sampling in December 1985, almost immediately. (App. 3 at No. 400.)

It is undisputed that by this time Texas Eastern understood that it would have to remediate many of its pits to clean the PCB contamination. (Dep. of Howard Homeyer, App. 449 at 134.) In this litigation, it now seeks to recover these remediation costs. A document prepared for Henry King, Texas Eastern's President, by his administrative assistants, dated November 5, 1985, states that "TE's insurance does not cover any costs of clean-up but any accident or emergency involving PCB's [sic] would be covered under the Corporation's liability insurance." (App. 324 at 2.) It is disputed whether this information was provided by Texas Eastern's Risk Management Division, but it does establish that Texas Eastern's senior management did consider the potential insurance ramifications of an on-site remediation of PCB contamination.

The Carriers observe that the Special Master[20/] concluded that Texas Eastern anticipated litigation with EPA no later than May 1985, and entered into negotiations with EPA no later than August 1985. (Special Master's "Report and Recommendation No. 2" at 14, Document No. 383.) The Carriers assert that this evidence establishes that Texas Eastern knew, or should have known, that EPA was making a claim against Texas Eastern because of an occurrence which was *likely* to give rise to a significant

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[20/] Arlin Adams, formally a judge on the Third Circuit Court of Appeals, was the special master assigned to this case for the purpose of resolving certain discovery disputes involving claimed attorney-client and work-product privileges.

claim. Texas Eastern responds that these negotiations did not involve "occurrences" as defined by its insurance policies, and that no notice to the insurance carriers was required, because any potential litigation would *not* have concerned third-party damage. (Cody Decl., TApp. 214 at ¶¶ 7, 8.) Although Texas Eastern disavows that it is claiming indemnity for the cleanup costs unassociated with third-party damages,[21/] it is clear from all of its submissions that Texas Eastern is seeking complete indemnification for all costs it has incurred and will incur in the actual PCB cleanup. Thus, it would appear that at least by May 1985, Texas Eastern should have notified its primary and excess CGL carriers of the likelihood of a claim or claims, if it is to recover any of these remediation costs.

6. *1986*

By February 18, 1986, Weston delivered a draft report of the six-site survey to Texas Eastern. (App. 341.) The report clearly establishes that PCBs were found in the drainage swales and surface water bodies of the unlined earthen pits, and that the potential for off-site migration existed. (*Id.* at 001363937.) This is uncontradicted evidence that Texas Eastern was, at a minimum, aware of the potential for off-site migration as of February 1986.

Texas Eastern met with EPA officials on April 30, 1986, to present the results of Weston's investigation and expressed an interest in entering into a consent agreement to

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[21/] Texas Eastern, of course, believes that all costs incurred pursuant to the EPA Consent Decree are associated with third-party damage. I reject this view as discussed under "Owned Property." *See supra* part XI.

clean up the pits. (App. 76.) Texas Eastern maintains, however, that this settlement, and EPA's concern about the pits, did not include any consideration of off-site migration or off-site remediation.[92/] Texas Eastern's knowledge that PCBs were found in the swales and surface liquids of the pits, and its knowledge that, over the course of years, pit liquids had migrated onto third-party properties, for which claims were made and compensation paid (albeit not expressly for PCB contamination), certainly alerted Texas Eastern to the potential for PCB contamination claims being made in the future. Although Texas Eastern claims that it did not know PCBs could or would migrate from the pits, certainly, in light of all that it did know, it had reason to suspect the potential for migration and the likelihood of future claims by third-party landowners.

In May 1986, Texas Eastern requested that Weston expand its pit survey to include 54 additional compressor station sites. (TRSOF ¶ 354.) Texas Eastern received the initial results of this 54-site survey in December 1986, and ultimately forwarded the final results to EPA in March 1987. The March 1987 report clearly indicated that off-site contamination had occurred at a number of compressor station sites. (*See, e.g.*, Dep. of Bradford Cushing, App. 654 at 367-72 (relying solely on the March 1987 Weston 54-site survey final report to support his opinion that off-site migration of PCBs had occurred at the

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92/ In fact, it is Texas Eastern's position that EPA did not make any specific cleanup demands at any time prior to April 1987. (Church Decl., TApp. 191 at ¶ 9.) EPA's failure to demand an immediate cleanup may be explained, in part, by the fact that the Weston report which Texas Eastern presented to EPA intentionally and deliberately deleted all of the references to potential off-site migration contained in the February 1986 draft. (Ins.' Mem. in Opp'n Summ. J.—Late Notice at 10-11.)

Wheelersburg, Ohio compressor station.)) In the Carriers' view, the only reasonable inference that can be drawn from the March 1987 final report is that Texas Eastern knew, or should have known, based on the December 1986 preliminary report, that off-site PCB migration had occurred. Supporting the Carriers' view is Texas Eastern's admission, at oral argument, that the initial results should have alerted Texas Eastern to the fact that off-site PCB contamination had occurred at a number of compressor station sites. (*See infra* p. 163 note 97.)

In December 1986, Texas Eastern proposed a cleanup plan to EPA. (TRSOF ¶ 375; App. 3 at No. 437.) Justice Department representatives made it clear to Texas Eastern that it would require a judicially enforceable consent decree to result from these discussions. (Dep. of Carol Dinkins, App. 362 at 46.) By this time, Texas Eastern was committed to remediating the PCB contamination in its unlined earthen pits and the only material dispute between Texas Eastern and EPA was the extent of the cleanup and the form of the agreement which would be required.

In 1986, Lester Rosenberg, one of Texas Eastern's insurance brokers, began to assemble a list of CGL insurance policies purchased by Texas Eastern beginning with July 1, 1963. (App. 360.) The Carriers contend that this is evidence of Texas Eastern's intent to notify the Carriers of the remediation agreement with EPA. Texas Eastern responds that this was only part of a routine Texas Eastern Insurance Department practice to prepare historical summaries of insurance coverage. Neither party has offered evidence sufficient to establish the authenticity of either explanation.

The Carriers have further suggested that on July 3, 1986, a Texas Eastern Insurance Department employee

discussed Texas Eastern's PCB problem with Mr. Rosenberg, stating that there was third-party damage at multiple sites. (Ins.' Mot. Summ. J.—Late Notice at 13.) At Mr. Rosenberg's deposition, he did not remember having such a conversation and the parties have offered no other evidence which establishes, with undisputed facts, whether such a conversation ever took place. (*See* SOF ¶ 363; App. 355; Dep. of Lester Rosenberg, App. 302 at 1106-10.)

In December 1986, Texas Eastern received, from its insurance agents Querbes & Nelson, a list of claim notification information and a summary of policy limits and insurers. (TRSOF ¶ 383; App. 366.) Despite this, notice was not given to the Carriers for another eight months.

7. *1987*

On February 21, 1987, the Houston Chronicle published an article detailing Texas Eastern's PCB-related problems. (App. 370.) Having read the article, the Carriers contend that John Dwinell, an Aegis claims attorney, contacted Texas Eastern Claims Manager, Maynard Williams. Mr. Williams informed Mr. Dwinell that the reported PCB matter did not concern Aegis. (Dep. of John Dwinell, App. 373 at 36-37.) Mr. Williams testified that he did not recall the exact conversation, but he testified that "it would be sort of ludicrous of me to tell someone that they are not going to be involved in something." (Dep. of Maynard Williams, TApp. 34 at 235.) He also stated that he recalled Dwinell telling him that Aegis would cover third-party actions but not anything on Texas Eastern's own property. (*Id.* at 236.)

Texas Eastern's Insurance Manager, James Farley, testified that Texas Eastern considered giving notice in

February 1987, (Dep. of James Farley, App. 459 at 600-05), and that the Risk Management Department was being briefed weekly on the progress of the EPA discussions. (*Id.* at 606-07.) However, precisely what the Insurance Department was receiving notice of is hotly disputed by the parties and there are no undisputed facts on which to rely.[23/]

Texas Eastern contends that its Insurance Department personnel were unaware of any third-party threat in late 1986 and early 1987. Stephen C. Mulliken, the Manager of Texas Eastern's Insurance Department, testified at his deposition that in 1987 he understood that Texas Eastern was negotiating with EPA about the cleanup of PCBs on Texas Eastern's own property and that this would not involve the Corporation's third-party liability policies. (Dep. of Stephen Mulliken, TApp. 2 at 252, 284-89.) James Farley expressed a similar opinion at his deposition. (Dep. of James Farley, TApp. 1 at 153-57, 164, 179, 472, 499.) It was only in April and May 1987, that the Insurance Department began to consider the PCB problem as a potential insurance matter.[24/]

On March 17, 1987, Texas Eastern officials testified before a United States Senate Subcommittee concerning Texas Eastern's PCB problem and the status of its

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[23/] This is relevant because certain F & C policies required notice only after Texas Eastern's Insurance Department became aware of an "occurrence or claim." (*See supra* p. 139.)

[24/] Apparently, it is undisputed that the Insurance Department was aware that Texas Eastern had an on-site PCB problem. The reasonableness of the Insurance Department's action, after its personnel learned about the potential off-site harm, should take that knowledge into account.

settlement discussions with EPA. (App. 2 at 1, 13.) Shortly thereafter, the Carriers contend that settlement negotiations with EPA became intensive. Texas Eastern responds that prior to April 1987, EPA never insisted that Texas Eastern consider any risks of off-site contamination, and never insisted that cleanup levels be based on EPA's "risk assessment" with respect to harm caused or threatened to human health and the environment. According to Texas Eastern, this was also the first time that EPA demanded that Texas Eastern enter into formal negotiations to discuss specific cleanup demands. (TSOF ¶ 111; Church Decl., TApp. 191 at ¶ 9.) Even at this late date, Texas Eastern delayed notifying its insurance carriers for over four months.

On August 18, 1987, Carol Dinkins, Texas Eastern's attorney and chief negotiator, wrote a letter to David Batson, EPA's Chief Negotiator, outlining certain proposals made by Texas Eastern to settle the pit remediation issues with EPA. (App. 382.) I would not characterize this as an "agreement," but it clearly establishes that Texas Eastern had given the remediation issue significant consideration by this time in 1987.

According to Texas Eastern, after the Senate hearings, the Insurance Department began an investigation to determine the extent of the PCB contamination and to determine what insurance coverage was potentially available for the Corporation. (Dep. of James Farley, TApp. 1 at 436-37.) On August 19, 1987, Texas Eastern finalized its "notice of claim" letter, and mailed the letter to the Carriers several days later. (TRSOF ¶ 414.) This was the first formal written notice that any of the insurance carriers received.

Texas Eastern was, at a minimum, obligated to give the Carriers written notice (1) "as soon as practicable" upon the happening of an "occurrence" if it appeared likely to give rise to a claim—even if no claim had yet been presented to Texas Eastern, and (2) "with full particulars" of a claim "on account of such occurrence," once a claim was made. Texas Eastern admittedly did neither until August 19, 1987.

C. *Texas Law*

Texas law views the notice requirement as a condition precedent to coverage and "failure to perform the condition constitutes an absolute defense to liability on the policy." *Dairyland County Mut. Ins. Co. v. Roman*, 498 S.W.2d 154, 157 (Tex. 1973). This is true even if the insurer has actual notice of the loss. *Dairyland*, 498 S.W.2d at 157; *Employers Casualty Co. v. Mireles*, 520 S.W.2d 516, 518 (Tex. Civ. App. 1975) (writ refused n.r.e.).

The burden is on the insured to show that it has fulfilled all conditions precedent contained in the policies. *Trevino v. Allstate Ins. Co.*, 651 S.W.2d 8, 11 (Tex. Ct. App. 1983) (writ refused n.r.e.). *See also Dairyland*, 498 S.W.2d at 158. Thus, Texas Eastern must establish by admissible evidence that it gave notice in accordance with the policy provisions, or provide a reasonable explanation for its delay. Texas Eastern contends that its notice requirement accrued in April 1987 and that it provided notice "as soon as practicable" in August 1987.

The terms "as soon as practicable" or "immediately," as used in a notice provision, have been construed to require notice "within a reasonable time." *Broussard v. Lumbermens Mut. Casualty Co.*, 582 S.W.2d 261, 263 (Tex. Civ. App. 1979); *McPherson v. St. Paul Fire &*

Marine Ins. Co., 350 F.2d 563, 566 (5th Cir. 1965). *See also, New Amsterdam Casualty Co. v. Hamblen*, 190 S.W.2d 56, 58 (Tex. 1945). I interpret this to mean that the insured must display the degree of diligence which a reasonably prudent person would exercise under the same or similar circumstances. This necessarily requires an inquiry into what was reasonable under the circumstances of this particular case. *See Broussard*, 582 S.W.2d at 263 ("[W]hat is a reasonable time depends upon the facts and circumstances in each particular case.")

In this regard, "[t]he age, experience, capacity and knowledge of the insured are . . . circumstances to be considered in determining whether the required notice was given as soon as practicable." *Dairyland*, 498 S.W.2d at 158. *See also McPherson*, 350 F.2d at 567. Texas Eastern is a sophisticated corporation with a large Risk Management Department. Therefore, it should be held to a high standard when interpreting the reasonableness of the delay in providing notice to the Carriers.[25/] Texas Eastern knew about the potential for third-party claims and had assembled all CGL policies potentially involved by no later than December 1986, a period of eight months before notice was given.

Even a sophisticated insured is not expected to give notice until it knows of an "occurrence" that is likely to give rise to a claim under its insurance policies. *Ogden*

[25/] The question of whether notice is reasonable is usually a question of fact but if the facts are undisputed the question then becomes one of law. *Klein v. Century Lloyds*, 275 S.W.2d 95, 97 (Tex. 1955); *Broussard*, 582 S.W.2d at 262; *Continental Sav. Ass'n v. United States Fidelity & Guar. Co.*, 762 F.2d 1239, 1243 (5th Cir.), *amended on other grounds*, 768 F.2d 89 (5th Cir. 1985) (citing *Klein*, 275 S.W.2d at 97).

Corp., 924 F.2d at 43; *Employers Casualty Co. v. Scott Elecs. Co.*, 513 S.W.2d 642, 645-46 (Tex. Civ. App. 1974). Under Texas law, whether an insured knows or should have known of an occurrence is determined by an objective test. *Texas Glass & Paint Co. v. Fidelity & Deposit Co.*, 244 S.W. 113, 114-115 (Tex. Comm'n App. 1922).

Courts in Texas have repeatedly ruled that relatively short delays can be unreasonable, and that the insurer is, therefore, excused from defending and indemnifying the insured. *See, e.g., Klein v. Century Lloyds*, 275 S.W.2d 95, 97 (Tex. 1955) (thirty-four day delay in providing notice does not constitute notice given as soon as practicable); *Allen v. Western Alliance Ins. Co.*, 349 S.W.2d 590, 594 (Tex. 1961) ("We hold that as a matter of law the failure to give notice for 107 days, under the circumstances of this case, did not constitute the giving of notice 'as soon as practicable' after the accident."); *Trinity Univ. Ins. Co. v. Weems*, 326 S.W.2d 302, 304 (Tex. Civ. App. 1959) (three and one half month delay does not constitute notice given as soon as practicable); *Mireles*, 520 S.W.2d at 522 ("In the absence of waiver or special circumstances not present here, [the insured's] delay of over six months [six and one half months] is not notice as soon as practicable as a matter of law."); *Broussard*, 582 S.W.2d at 263 ("The delay of twenty months in giving notice of [the claim] to the insurance companies did not constitute giving notice 'as soon as practicable' as required by the insurance policies."); *Kellum v. Pacific Nat'l Fire Ins. Co.*, 360 S.W.2d 538, 542 (Tex. Civ. App. 1962) (writ refused n.r.e.) (one year delay not notice "as soon as practicable"). *See also McPherson*, 350 F.2d at 565-67 (fifty-four days is not notice "as soon as practicable").

Courts in other jurisdictions have strictly enforced notice provisions in environmental cases. *In American Home Assurance Co. v. Republic Ins. Co.*, 788 F. Supp. 214 (S.D.N.Y. 1992), American Home Assurance Company (American), a primary insurer, sued Republic Insurance Company (Republic) and United National Insurance Company (United), excess carriers, for contribution to a settlement agreement entered into by American on behalf of the insured. In granting the excess carriers' motion for summary judgment on the ground of late notice, the district court held that a "ten month delay from the insured's knowledge of its exposure to the notification of its insurers violated the timely notice of occurrence requirement of those policies." American Home Assurance, 788 F. Supp. at 218.

The court further observed that "even a one month delay" between the time that American was advised of a likely recovery and when it sent notice to Republic and United of the claim "failed to meet the policies' requirement that notice be afforded 'as soon as practicable,' particularly because during that time settlement negotiations obviously bearing on [Republic and United] were being conducted without their knowledge . . . ." *American Home Assurance*, 788 F. Supp. at 218. Similarly, the Carriers have claimed in the present litigation that Texas Eastern conducted extensive negotiations with EPA long before it gave notice to either its primary or excess insurers.

In *Olin Corp. v. Insurance Co. of N. Am.*, 743 F. Supp. 1044 (S.D.N.Y. 1990), *aff'd*, 929 F.2d 62 (2d Cir. 1991), the district court concluded that an insured's one year delay in providing notice constituted a violation of the terms of the insurance policy's notice provision. *Olin*, 743 F. Supp. at 1055. As in *Olin*, the Carriers contend that Texas Eastern was aware of its potential liability long

before it notified its Carriers. According to the Carriers, at a minimum, Texas Eastern should have provided notice at least by August 1985, when it began negotiating with EPA about the remediation of some of its unlined earthen pits.

D. *The Applicable Facts*

The parties' inability to agree on the nature of Texas Eastern's claim makes Texas case law difficult to apply in the present case. Texas Eastern has repeatedly asserted that it is not claiming recovery for any of the costs which it did not, or will not, incur because of third-party property damage, third-party personal injury, or third-party bodily injury. I have previously concluded that the relevant occurrence that could trigger liability in this litigation is third-party damage. Thus, providing Texas Eastern with the maximum possible extension of time, the duty to notify would mature no later than when Texas Eastern knew of actual off-site PCB migration or of the likelihood that off-site PCB harm or contamination had occurred. Unreasonable delay will, for the purposes of the present motions, be decided from that point forward. However, in determining what is a reasonable time, the known magnitude of the problem and Texas Eastern's own knowledge of the long existing on-site PCB contamination are relevant factors.

The undisputed evidence is insufficient to establish that EPA made a "claim" against Texas Eastern during the years 1981 through 1985. A claim is the assertion of a legal right through a specific demand, not merely notice of a potential problem. *Winkler v. National Union Fire Ins. Co.*, 930 F.2d 1364, 1367 n.4 (9th Cir. 1991). Although EPA was actively discussing Texas Eastern's future responsibilities regarding the pits, the evidence does not conclusively

establish that EPA demanded that Texas Eastern clean up any property.

The Carriers have offered insufficient undisputed evidence to establish that Texas Eastern was aware that PCBs were migrating off-site and contaminating third-party property prior to April 1986. The Carriers have, however, provided ample evidence that Texas Eastern was aware, for at least five years prior to giving notice to the Carriers, that it had a significant on-site PCB problem. Therefore, once Texas Eastern understood that PCBs were actually migrating, or understood the reasonable likelihood of migration, its obligation to provide notice should have accrued very shortly thereafter.

The first time Texas Eastern appears to have considered the potential migration of PCBs was in its initial meetings with representatives of Weston in late 1985. The initial six-site sampling program was designed to determine the extent of PCB contamination in Texas Eastern's pits, including the potential for off-site migration. (Dep. of Manmohen Bhatla, App. 651 at 19-20, 98-99.) The suggestion to check for migration was apparently made by Weston representatives. (*Id.*) Notes from the initial discussions between Texas Eastern and Weston establish that the parties also discussed the depth of groundwater and the proximity of groundwater to streams at various locations. (App. 328 at 2.)

Bradford S. Cushing, Texas Eastern's environmental expert, testified that the possibility of off-site migration was discussed with Texas Eastern representatives, including H. Douglas Church and Robert Salzer. (App. 653 at 373-76, 379-82, 675-81.) Mr. Cushing also testified that the results of the initial six-site survey indicated that there was the

possibility of PCB migration to areas off the compressor station sites. (App. 653 at 679.)

Texas Eastern responds that it did not know of any off-site migration during this time. It offers H. Douglas Church's letter to EPA, dated April 25, 1986, in which he explains that Texas Eastern had installed silt fencing to prevent migration of contaminated sediment to surface water bodies. (App. 171 at 5.) This letter confirms that Texas Eastern, at a minimum, understood the *potential* for, if not the probability of, off-site migration, by April 1986. In addition, the Carriers offer what is represented to be an earlier draft of this letter in which Texas Eastern wrote:

> The presence of PCBs in the surface waters and drainage swales indicates that *PCBs may be migrating from station sites*. Remedial actions were initiated the week of April 14, 1986 *to reduce further off-site migration potential* through the installation of filter fabric, a sedimentation control measure, at three sites identified by the pilot study.

(App. 339 at 7) (emphasis added.) This draft certainly suggests that Texas Eastern's senior management understood that off-site migration was probably taking place at some of its compressor station sites as early as April 1986; over one and one-third years before Texas Eastern provided notice to the Carriers.[26/]

[26/] On March 30, 1987, it appears that Texas Eastern gave notice to an insurance company not party to this litigation (A.C.E.) of a potential

(continued...)

This evidence clearly contradicts the litigation affidavits offered by Texas Eastern to establish that it did not have any knowledge of off-site migration until April 1987. For example, H. Douglas Church declared that until 1987, Texas Eastern did not recognize that actual off-site migration had occurred. (Church Decl., TApp. 191 at ¶ 8). However, the draft of his April 25, 1986 letter to the EPA explicitly contradicts this. Derrill Cody, Executive Vice President of Texas Eastern Corporation from June 1986 through December 1989, declared that it was not his understanding that Weston's initial sampling program indicated off-site PCB contamination. (Cody Decl., TApp. 214 at ¶ 5.) The February 1986 draft report of the Weston six-site survey clearly shows that Mr. Cody was mistaken.

Texas Eastern also consistently downplays the Carriers' offers of record proof establishing that Texas Eastern was aware of at least some "isolated" instances where Weston samples discovered off-site migration. First, Texas Eastern argues that there is no evidence that Insurance Department personnel were aware of these findings. I will explain, *infra* pp. 164-66, that in most cases the actual knowledge of the Insurance Department is not relevant because Texas Eastern had a continuing duty to keep its Insurance Department advised of relevant corporate information which should have included information concerning the off-site migration of PCBs.

Second, Texas Eastern often relies on the fact that, in its view, the potential for off-site migration and third-party

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[26](...continued)
claim arising out of the discovery of PCBs in drinking well water near one of Texas Eastern's compressor stations. (App. 367.) This is approximately five months before Texas Eastern gave the Carriers involved in this litigation notice of any "occurrence."

harm was minute, insignificant, and extremely localized and therefore did not trigger any duty to notify the Carriers. (*See, e.g.*, TE's Reply in Supp. Summ. J.—Late Notice at 14: "[T]here is no evidence that any operational employee considered the potential for offsite PCB migration to be significant: the silt fences were merely a routine precaution against soil erosion, which was then thought to be the only way that PCBs could move offsite.") As I have explained, Texas Eastern was aware that it had a significant on-site PCB problem many years prior to the discovery of even the potential for off-site contamination, and Texas Eastern knew that EPA would require a costly cleanup. Thus, even the slightest hint of off-site migration would have required Texas Eastern to provide the Carriers with prompt notice because of the potential magnitude of the PCB contamination problem and the likelihood of a future claim.

It is therefore established, by undisputed record evidence, that Texas Eastern both understood the potential for off-site migration, and knew, at least as of April 1986, that *some* off-site migration had *probably* occurred. These events are highly relevant in establishing the time when Texas Eastern's obligation to provide notice accrued, because they specifically relate to the off-site, as opposed to on-site, migration of PCBs. Although I am tempted to conclude, as a matter of law, that Texas Eastern should have provided notice in April 1986, I have instead chosen December 1986, the date on which Texas Eastern received the results of Weston's 54-site survey, as the date on which Texas Eastern's notice obligation matured, because that is the date on which Texas Eastern should have clearly understood, as a matter of law, the potential for off-site

PCB migration and the likelihood that such migration had actually occurred.[27]

It is my duty to determine whether, after the obligation to provide notice had accrued, the insured provided notice within a reasonable amount of time under the circumstances. I will therefore address Texas Eastern's arguments in support of its allegation that notice was provided within a reasonable time.

First, Texas Eastern contends that the August 1987 notice was provided within a reasonable time because, in Texas Eastern's view, no "occurrence," as defined by its insurance policies, took place until after it had notice of the likelihood that off-site harm was taking place. This argument is inapposite, as I have concluded that Texas Eastern need not have provided notice before it was aware of the likelihood of off-site migration.

Second, Texas Eastern contends that at least as to the F & C policies effective from 1967 to 1981, the August 1987 notice was provided within a reasonable time because

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[27] This point was made clear at oral argument in the statements of Mr. Nickels, counsel for Texas Eastern, in response to my questions:

> THE COURT: And when was that, the Weston [54-site survey] report?
>
> MR. NICKELS: It was presented formally to the EPA, I believe, in March or April of 1987.
>
> THE COURT: Well, when was it presented to Texas Eastern? MR. NICKELS: December, '86.
>
> THE COURT: All right. Now, at that time you certainly knew that they [PCBs] were emanating off-site, didn't you, or had reason to believe that they were?
>
> MR. NICKLES: We had reason to believe that, that is right your Honor.

Tr. of Hr'g on Mot. for Summ. J., January 13, 1992 at 93-94.

notice to the Carriers was required only after notice of a "claim or occurrence" was received by its Insurance Department or by a Texas Eastern executive. The undisputed facts completely undermine Texas Eastern's argument. Although the Insurance Department might not have been on notice in the early 1980s, at least by April 1986, executive officers at Texas Eastern had notice of actual and potential third-party migration. (*See supra* pp. 160-61.)

Third, Texas Eastern contends that as to the F & C policies effective from 1981 to April 1988, the August 1987 notice was provided within a reasonable time because notice to the Carriers was required only after notice of a "claim or occurrence" was received by Texas Eastern's Insurance Department. Texas Eastern appears to believe that this policy language relieves it of the duty to inform its Insurance Department of those facts which are relevant to the performance of the Insurance Department's corporate task. It does not. Texas Eastern had a continuing duty to keep its Insurance Department informed of relevant corporate activities so that it could keep track of Texas Eastern's potential insurance claims.[28/]

Given the extensive nature of the known on-site PCB problem, Texas Eastern admits that it certainly would have been *prudent* for its senior management to have kept the Insurance Department informed of the PCB problems in the mid-1980s. (*See* Dep. of H. Douglas Church, App. 568 at

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[28/] The policy requirement that the Insurance Department be informed of the claim or occurrence must be read to include a duty on Texas Eastern's part to make its Insurance Department aware of relevant corporate activities. Otherwise, insureds could easily build "Chinese walls" around their insurance departments for the sole purpose of defeating insurance carrier defenses to coverage.

933-36.) In any event, once Texas Eastern's senior management understood that the PCBs were migrating off the compressor station sites, Texas Eastern's own guidelines would have required that the Insurance Department be informed.[99] For all of these reasons, I conclude that the Insurance Department was "informed" of the occurrence of off-site migration at least by the time Texas Eastern's senior management became aware of the migration.[100]

When all of the facts are taken into consideration, it is clear to me that Texas Eastern has provided no credible explanation for the eight month delay[101] (December 1986 to August 1987) in providing the Carriers with notice of the off-site migration and the potential claims that would likely arise out of that "occurrence." Texas Eastern was aware of the magnitude of its on-site PCB problem and it was aware

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[99] Stephen Mulliken, Director of Texas Eastern's Risk Management Department, testified at his deposition that Texas Eastern had guidelines in effect which required that all accidents, occurrences, or events that may lead to a claim, whether a formal claim was presented or not, should be immediately reported through the field offices to the Claims Department in Houston. (Dep. of Stephen Mulliken, App. 261 at 258.)

[100] Texas Eastern contends that only the Insurance Department had the requisite skill to make the subjective determination of when a claim was "likely" to involve a particular excess policy. Nothing in the policy language requires this result and I find Texas Eastern's argument to be wholly without merit. Senior management was qualified to make decisions concerning the likely involvement of excess carriers on individual claims. In addition, the duty to inform the Insurance Department of important corporate matters would include informing it of the known off-site migration of pollutants and contaminants.

[101] It should be clear that December 1986 merely represents the latest possible date on which undisputed evidence establishes that Texas Eastern's notice obligation accrued. I previously indicated that April 1986 could, in all likelihood, also have been chosen.

of the likelihood for off-site migration by the end of 1986. Notice should have been provided to its Carriers at that time. Eight months thereafter is, as a matter of law, not "as soon as practicable" and not within a reasonable amount of time.[102/]

E. *Prejudice*

Under Texas law, the Carriers contend that they do not need to demonstrate that they have been prejudiced by Texas Eastern's failure to provide timely notice.

However, the Texas State Board of Insurance approved an "Amendatory Endorsement" which is "applicable to all general liability policies issued or delivered in Texas" which states that a notice provision is operative only where an insurer proves that it has been prejudiced by the delay. (App. 460.) The effective date of the endorsement is April 1, 1973. *Members Ins. Co. v. Branscum*, 803 S.W.2d 462, 467 (Tex. Ct. App. 1991). The Carriers contend that, by its terms, the endorsement does not apply to excess liability policies, or general liability policies neither issued nor delivered in Texas. I do not decide this issue, because I

[102/] Even if Texas Eastern's unsupported contention that it did not learn about the off-site migration of PCBs until April 1987 is accepted, I would still conclude that notice was late as a matter of law. Texas Eastern was clearly aware of the magnitude of its PCB problem in April 1987, and was negotiating with EPA to settle the issue of pit remediation. Although four months may appear to be a short period of time, Texas Eastern has advanced no meritorious explanation for the delay. The period from April to August 1987 was a crucial time for the Carriers to be involved in the settlement process and Texas Eastern's delay deprived the Carriers of this opportunity. Under Texas law, Texas Eastern had a duty to promptly notify the Carriers. Notice, after a four month delay, fails to be notice within a reasonable time. (*See* cases cited *supra* pp. 155-57.)

conclude that Texas Eastern's failure to timely notify the Carriers prejudiced them as a matter of law.[103/]

The Carriers bear the burden of proving that they were prejudiced by Texas Eastern's late notice. *Branscum*, 803 S.W.2d at 467. "The purpose of the notice requirement is to enable the insurer to promptly investigate the circumstances of an accident so that it can prepare to defend any claim that may arise." *Stonewall Ins. Co. v. Modern Exploration, Inc.*, 757 S.W.2d 432, 435 (Tex. Ct. App. 1988). This includes the ability to interview witnesses while the facts are still fresh in their minds, to prevent fraud, and to enable it to form an intelligent opinion of its rights and liabilities under the policy. *Stonewall*, 757 S.W.2d at 435.

Courts in other jurisdictions have emphasized the importance of allowing the insurance company to control the proceedings including investigation, settlement, and litigation. For example, in *Metal Bank of Am., Inc. v. Insurance Co. of N. Am.*, 520 A.2d 493 (Pa. Super. Ct.), *appeal denied,* 536 A.2d 1332 (1987), the court explained that "the reason for [requiring] timely notice to the insurer is to enable it to gain early control of the proceedings and give it an opportunity to investigate and acquire information about the case." *Metal Bank*, 520 A.2d at 498. On the facts before it, that court concluded that the insured's late notice had denied the insurer all of this, particularly because a settlement between the insured and EPA was a *fait accompli* by the time the insured provided notice.

[103/] Prior to the 1973 enactment of the endorsement, no showing of prejudice was required. Thus, as to those policies written prior to April 1973, no prejudice need be shown.

In *West Bay Exploration Co. v. AIG Specialty Agencies*, 915 F.2d 1030 (6th Cir. 1990), the court concluded that the insured's failure to notify its insurer before disposing of the contamination source responsible for the damage for which the insured was seeking coverage, prejudiced the insured by denying it the opportunity to investigate the claim. The court noted that each of the insurance policies contained a pollution exclusion; by removing the pollution source, the insured "materially compromised the [insurers'] ability to present their most powerful defense to liability under the policy." *West Bay*, 915 F.2d at 1037. The court's rationale raises an additional purpose of the notice requirement: to allow the insurer to investigate an accident in order to determine whether *it* need provide the insured with any coverage at all. *See also Stonewall*, 757 S.W.2d at 435 (notice provision allows the insurer to ascertain *its* rights and liabilities under the policy).

The Carriers contend that Texas Eastern has waited so long to give them notice that important witnesses can no longer recall important events.[104/] More importantly, Texas Eastern's delay foreclosed any opportunity for the Carriers to play a meaningful role in the discussions with EPA and state agencies, participate in the development of the remedial and investigatory programs, or control in any way the costs for which Texas Eastern is now seeking indemnification. The Carriers have also suggested that Texas Eastern waived certain defenses to EPA's claims in the course of their initial negotiations.

[104/] Portions of depositions give credence to this argument. (*See, e.g., supra* pp. 149-50.)

Texas Eastern vigorously denies that the Carriers have established prejudice. First, Texas Eastern asserts that the negotiations between Texas Eastern and the EPA grew strained during August 1987 and came to a standstill at the end of the month, when EPA declared that it was preparing to file litigation. (TApp. 172.) According to Texas Eastern, in mid-September, only after having been assured that Texas Eastern's negotiating team would be "authorized to recommend a conceptual agreement" to Texas Eastern's management, EPA advised Texas Eastern that it would postpone the filing of litigation "for a short while" in order to permit continuation of the settlement discussions. (TApp. 173.) The parties subsequently entered into a non-binding "Agreement in Principle" on November 9, 1987. The EPA Consent Decree was filed in June 1988. (App. 474 at 10-11.) Thus, Texas Eastern contends that the Carriers had ample time after they received notice to participate in the negotiation process.

Texas Eastern's contentions are unavailing. The simple fact that negotiations became strained in August 1987 did not undue all of the work done prior to that date. Certainly Texas Eastern knew that it faced very substantial liabilities, and that EPA would not release it from those liabilities absent a settlement agreement or litigation. As Texas Eastern admitted, shortly after the "impasse," Texas Eastern resumed negotiations with EPA, and within months settled on an Agreement in Principle. By the time the Carriers received notice, the matter was for all intents and purposes a *fait accompli*, or in more modern vernacular, it was a "done deal."

In a September 2, 1987 letter to EPA, Carol Dinkins summarized "the relative positions of the parties as of August 28, 1987." (App. 646.) The letter included a list of thirty-five items on which agreement had been reached, and

Ms. Dinkins commented that the "list is impressive, both for the number of items that it contains and the magnitude of the undertaking that it represents." (App. 646 at 001371187.) Texas Eastern had already agreed to pay a civil penalty and oversight costs, although the amount was yet to be agreed upon. (*Id.* at 001371184-85.) Given these undisputed facts, I am convinced that the Texas Supreme Court would hold, as a matter of law, that the Carriers were prejudiced by Texas Eastern's late notice.

Second, Texas Eastern contends that even if the Carriers establish that they have suffered some prejudice, the Carriers must prove that they could have changed the result had proper notice been provided. This is not the law of Texas. Texas may require prejudice, but it has expressly rejected the application of a "substantial prejudice" standard. *Branscum*, 803 S.W.2d at 467. Under Texas law, an ordinary showing of prejudice is sufficient to invalidate coverage.

Third, Texas Eastern contends that it did not receive the first of many private third-party claims until after August 1987, and it received most of the governmental claims (state agency claims) after that date as well. Therefore, the Carriers could have participated in the defense of these lawsuits after they received notice.

The Carriers respond that Texas Eastern entered into a voluntary consent decree with the Commonwealth of Pennsylvania in April 1987, in which Texas Eastern agreed to "assess any contamination at the Pennsylvania sites and to remedy that contamination expeditiously." (App. 227C at 6.) Thus, prejudice has clearly been established concerning the Pennsylvania claim. More importantly, however, I conclude that the Carriers were sufficiently prejudiced by Texas Eastern's handling of the EPA Complaint and the

resulting EPA Consent Decree, the cost of which constitutes the majority of Texas Eastern's claim against its insurance carriers, that isolated instances where the Carriers may have received timely notice of the actual filing of a claim are insufficient to cure the overall prejudice which the Carriers initially suffered.[105/] By the time Texas Eastern gave notice, remedial efforts, testing, and monitoring had begun, and schedules and methodologies to characterize the sites had been established. Most importantly, Texas Eastern had already presented to EPA its proposed settlement terms, and thus completely destroyed any meaningful opportunity for the Carriers to shape the negotiations with EPA. The record makes it abundantly clear that Texas Eastern never wanted the Carriers to interfere with what was a carefully negotiated settlement with EPA and waited until the

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[105/] For example, it is clear from the record that Texas Eastern likely relied on the environmental studies and its consultations with EPA concerning the contamination on its own property to form its opinions about the contamination which was the subject of the state agency and private third-party claims. The Carriers should have had an opportunity to participate in the decisions concerning the studies and the overall approach which Texas Eastern decided to employ with regard to its PCB contamination problems. Texas Eastern's late notice denied the Carriers this important opportunity and thereby prejudiced the Carriers.

As for the private third-party claims, all but two of these claims are not presently before this court. However, because Texas Eastern was aware, for a long period of time, of the likelihood of private third-party claims by reason of the admitted off-site migration of PCBs, even if the exact identities of the claimants were unknown, the Carriers were equally prejudiced by being unable to make their own investigation and take action to minimize future private party claims. See, e.g., Olin Corp. v. Insurance Co. of N. Am., No. 91-9155, 1992 WL 114441, *5 (2d Cir. June 1, 1992) (The filing of an initial lawsuit "would surely have alerted a reasonable person to suspect that other claims by varied plaintiffs . . . might follow.")

settlement was substantially agreed upon before providing any notice to the Carriers.

Texas Eastern failed to provide the Carriers with timely notice of the "occurrences," the claims, and the likelihood of claims arising from the "occurrences," thereby violating a condition precedent to receiving insurance coverage. The carriers have established that they have suffered prejudice because of this delay. Texas Eastern has failed to provide an adequate excuse, or even any plausible explanation, for the unreasonable delay.

For all of these reasons, the Carriers' joint partial motion for summary judgment on the issue of "Late Notice" will be granted and Texas Eastern's cross-motion will be denied. By reason of the late notice, all of Texas Eastern's claims must fail.

XIV. DUTY TO DEFEND

Texas Eastern contends that Fidelity had a duty to defend it against the threatened EPA action and the various state and private third-party actions, and has moved for summary judgment on this ground.[106/] Fidelity responds that under Texas law it had no duty to defend because the claims made against Texas Eastern were not covered by its insurance policies, and even if it did have a limited duty to defend, that duty would be defined by its duty to indemnify Texas Eastern against losses, thereby making Texas Eastern's motion for summary judgment premature.

[106/] No claim is being asserted against the excess insurance carriers on this ground.

A. *The Policy Language*

Although Texas Eastern and F & C vigorously disagree about whether all or some of the eight insurance policies which F & C issued to Texas Eastern, beginning in 1961 and ending in 1988, require F & C to defend Texas Eastern, both parties agree that if the duty to defend exists at all, it exists pursuant to the policies written between 1961 and 1973, which contain a duty to defend clause which can correctly be characterized as "traditional."[107]

The language of the policies can be summarized as follows:

> With respect to such insurance as is afforded by this policy, the company shall . . . defend any suit against the insured alleging such injury or destruction and seeking damages on account thereof, even if such suit is groundless, false, or fraudulent . . . .

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[107] The parties dispute what the precise nature of Fidelity's duty was under the insurance policies issued from 1973 to 1988. The contracts are so confusing that counsel for Texas Eastern professed to staying up all night before oral argument attempting to understand them but was unable to do so. Having read the contract language, I have little doubt that counsel was telling the truth. Because I conclude that F & C had no duty to defend even under a more traditional duty to defend clause, I do not reach the issue of F & C's obligations under these later clauses, which were clearly more restrictive and limited than the usual duty to defend clauses contained in CGL policies.

B. *Texas Law*

Under Texas law, an insurer's contractual duty to defend is ordinarily determined solely from the face of the pleadings without reference to the truth or falsity of such allegations and without reference to facts outside the pleadings. *Heyden Newport Chem. Corp. v. Southern Gen. Ins. Co.*, 387 S.W.2d 22, 24-25 (Tex. 1965); *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116, 119 (5th Cir. 1983). The duty arises when a comparison of the complaint and the insurance policy reveals that at least one of the allegations, if proven to be true, would state a cause of action within the terms of the policy. *Rhodes*, 719 F.2d at 119. In applying this "pleadings only" or "four corners" rule, "the court may indulge the most liberal interpretation of the allegations of which they are susceptible and doubts as to the import of the allegations are to be resolved in favor of the insured and coverage." *Continental Sav. Ass'n v. United States Fidelity & Guar. Co.*, 762 F.2d 1239, 1243-44 (5th Cir.), *amended on other grounds*, 768 F.2d 89 (5th Cir. 1985); *Heyden*, 387 S.W.2d at 26.

In the ordinary situation, an insurer must make a determination after a complaint has been filed against its insured as to whether any of the stated allegations, if ultimately found to be true, could potentially state a claim that would result in a covered loss under the insurance policy. If the insurer determines that a colorable claim has been made, then the duty to defend arises. If the insurer properly determines that no covered claim has been made, then there is no duty to defend.

The Texas courts have deviated from an orthodox application of the four corners rule, and looked beyond the pleadings in order to determine whether the insurer has a duty to defend, in cases where the issue is whether the

claims, even if proven true, would not be covered under the policy of insurance. For example, in *Gonzales v. American State Ins. Co.*, 628 S.W.2d 184 (Tex. Ct. App. 1982), the court explained:

> Where the insurance company refuses to defend its insured on the ground that the insured is not liable to the claimant, the allegations in the claimant's petition control, and facts extrinsic to those alleged in the petition may not be used to controvert those allegations. But, where the basis for the refusal to defend is that the events giving rise to the suit are outside the coverage of the insurance policy, facts extrinsic to the claimant's petition may be used to determine whether a duty to defend exists.

Gonzales, 628 S.W.2d at 187. In *McLaren v. Imperial Casualty & Indem. Co.*, 767 F. Supp. 1364 (N.D. Tex. 1991), *aff'd in part and rev'd in part on other grounds*, No. 91-1254 (5th Cir. April 9, 1992) (unpublished opinion), the district court surveyed Texas law and concluded that the application of the allegations of the complaint rule

> is limited in [Texas's] reported cases to two kinds of situations. One is where the insurance company seeks to avoid the defense obligation on the ground that extrinsic facts establish that the insured is not liable in the underlying suit. . . .
> The second situation . . . is where the underlying complaint affirmatively

> alleges a set of facts that fall within an exclusion to the policy coverage or are otherwise outside of the coverage.

McLaren, 767 F. Supp. at 1372-73. The court explained that the rule had no application in situations where the insurer attempted to prove that it had no defense obligations at all. *Id.* at 1374. *See also*, *Blue Ridge Ins. Co. v. Hanover Ins. Co.*, 748 F. Supp. 470, 473 (N.D. Tex. 1990) ("The status of the 'insured' is to be determined by the true facts, not . . . incorrect facts that might be alleged by a personal injury claimant . . . .")

The New Jersey Supreme Court reached a similar conclusion under New Jersey law. In *Hartford Accident & Indem. Co. v. Aetna Life & Casualty Ins. Co.*, 483 A.2d 402 (N.J. 1984), the New Jersey Supreme Court observed that "'[t]he duty to defend is not a product of statute or of common law. It is solely a contractual undertaking of the insurer and it can be as limited or as broad as the insurer sees fit to provide through its policy.'" *Hartford*, 483 A.2d at 405 (quoting the trial court's opinion.)[108/] In interpreting the standard duty to defend clause, the court concluded that "'the duty to defend extends only to claims on which there would be a duty to indemnify in the event of a judgment adverse to the insured.'" *Id.*

The *Hartford* Court recognized that the general approach to the duty to defend problem obligated an insurer to defend an action whenever the complaint alleges a basis

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[108/] Texas law is in accord with this view of the duty to defend. *See, e.g., Whatley v. City of Dallas*, 758 S.W.2d 301, 304 (Tex. Ct. App. 1988) (writ denied) (the duty to defend is ordinarily a contractual undertaking defined by the insurance policy).

of liability within the covenant to pay. However, the court explained that when the duty "'depends upon a factual issue which will not be resolved by the trial of the third party's suit against the insured, the duty to defend may depend upon the actual facts and not upon the allegations in the complaint.'" *Hartford*, 483 A.2d at 406. In these cases, the court concluded that it was appropriate for a court to review facts outside of the complaint in order to determine whether the insurer has a duty to defend.

Texas Eastern urges me to reject this view of the duty to defend because it defeats the primary purpose of the four corners rule in that an insured will have to defend against the third-party claim and at the same time will have to prove to its insurance company that the allegations are potentially covered by its insurance. In Texas Eastern's view, an insured should not have to bear this burden at a time when what it needs most urgently is a competent defense against the third-party claimant.

I agree that an insured needs a competent defense; the question that I address here, however, is who should provide it. If the insurer has no duty to indemnify the insured because the allegations, even if true, would not be covered by insurance, then the insurer has every contractual right to refuse to defend its insured. If the insurer chooses, it may, of course, defend its insured with a reservation of rights concerning its ultimate responsibility to indemnify the claims if the claimant (against the insured) is victorious. The mere fact that the third-party claimant has failed to allege facts which would conclusively establish that the insurer does not have a duty to indemnify a particular claim should not alter the insurer's ability to prove that it has no contractual duty to defend. This is particularly true in a case such as the instant one where the insured's initial defense demand, concerning the EPA action, came before

any formal complaint was ever filed, and thus the precise nature of the allegations was unknown.

As the New Jersey Supreme Court explained in *Hartford*, "'[t]his is not to free the carrier from its covenant to defend, but rather to translate its obligation into one to reimburse the insured if it is later adjudged that the claim was one within the policy covenant to pay.'" *Hartford*, 483 A.2d at 406. Although this alters the nature of the duty to defend, it is an appropriate result because the contractual duty to defend is only one to defend suits involving claims which the carrier would have to pay if the claimant prevailed in the action. Although the Texas Supreme Court has never expressly adopted this test, I am convinced that it would do so if faced with this particular question.

This result is particularly appropriate given the unique nature of Texas Eastern's defense demand. In Texas Eastern's view, notice to F & C that it was involved in protracted negotiations with EPA concerning the resolution of imminent PCB-related claims was sufficient to invoke F & C's defense obligations. In the typical case, the defense obligation arises when a complaint is filed and the insurer is able to compare the complaint with its insurance contract and determine whether any of the allegations could potentially lead to a covered claim. Due to the nature of the claim involved in the instant case, F & C did not have the benefit of seeing the complaint before it was filed in June 1988, simultaneous with the filing of the Consent Decree.

In fact, even if F & C had the benefit of seeing the complaint, it is not entirely clear that it would have stated a covered cause of action. The complaint relies almost exclusively on allegations that Texas Eastern violated TSCA

and RCRA provisions and thereby caused PCB environmental contamination on property owned and operated by Texas Eastern. The complaint clearly indicates that the contamination occurred over a period of years. The complaint does not even mention or suggest damage or imminent risk to third-party property or third-party injury.[109/]

I have heretofore concluded that there are issues of fact as to whether there was an "occurrence" within the coverage of the CGL policies, thereby precluding summary judgment in favor of the Carriers on the "Occurrence" issue. Ordinarily this would lead to the conclusion that the EPA Complaint stated a potentially covered claim thereby triggering a duty to defend upon demand and notice by Texas Eastern.

However, when I consider extrinsic evidence available to F & C at the time its duty to defend arguably accrued, it is clear that it had no duty to defend Texas Eastern against the claims made by EPA. I have concluded that the notice

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[109/] Texas Eastern argues for an orthodox application of the four corners rule on the duty to defend issue, even though it relies very heavily on extrinsic evidence to prove that the complaint and the Consent Decree caused it to incur liability which can be linked to some third-party injury that is nowhere alleged in the EPA Complaint. Its reliance on the Hammerstrom affidavits is a good example. Texas Eastern relies heavily on these two affidavits to establish that EPA considered potential harm to third-parties when it determined the acceptable levels of contamination that could safely remain on Texas Eastern property after the remediation was complete. The affidavits were submitted to the court in support of the Consent Decree, not as a part of the original complaint. An application of the four corners rule would prevent the consideration of this piece of evidence, which I believe is crucial in order for Texas Eastern to establish that any of its response costs are recoverable from its third-party liability carriers.

provided by Texas Eastern to its Carriers, including F & C, was late and prejudicial to the Carriers as a matter of law, and will grant the Carriers summary judgment on this issue. As was explained in "Late Notice," *supra* part XIII.C, timely notice is a condition precedent for an insured to be entitled to coverage for any claim. Late notice makes all claims, whether or not potentially covered, uninsurable. *Klein*, 275 S.W.2d at 96; *New Amsterdam*, 190 S.W.2d at 58; *McPherson*, 350 F.2d at 566. As a result, no duty to defend ever accrued on or after the date of the late notice on August 19, 1987.[110/] Although F & C did not expressly move for summary judgment in its favor on the "Duty to Defend" issue, granting summary judgment on the "Late Notice" issue, in favor of all the Carriers, will eliminate any duty to defend that F & C might otherwise have had to defend Texas Eastern. Summary Judgment will therefore be entered in favor of F & C on the "Duty to Defend" issue.[111/]

110/ For the same reasons, any F & C policy containing a pollution exclusion clause also defeats Texas Eastern's contention that F & C has a duty to defend.

111/ I have concluded that F & C had no duty to defend Texas Eastern. However, a number of issues raised by the parties regarding F & C's liability in the event it is determined that it breached its duty to defend require brief comment.

In Texas Eastern's view, F & C's failure to defend would obligate F & C to pay all defense costs, and to pay all damage claims, including those claims not covered by the insurance policies, up to, and perhaps even exceeding, the policies' limits. In addition, F & C would be prohibited from challenging the reasonableness of the settlements entered into by Texas Eastern.

Texas law does not support the majority of these assertions. While it is apparently true that an insurer cannot challenge the reasonableness of a good faith settlement entered into after a breach of

(continued...)

Finally, concerning the Pennsylvania state agency action, I have found no evidence that Texas Eastern made a defense demand on F & C before settling with the PaDER in April 1987. As such, no duty to defend could have accrued. As to the other state and private third-party actions which are still a part of this litigation, I have previously concluded that the prejudice suffered by the Carriers due to the late notice affected more than just their ability to defend against the EPA claim. The late notice prevented them from adequately defending against all claims which followed. Specifically, the late notice prevented the Carriers from participating in Texas Eastern's initial cleanup decisions and from participating in the majority of Texas Eastern's negotiations with EPA. Although a number of the state and third-party claims were filed after Texas Eastern first provided notice to the Carriers, it would be inequitable to allow Texas Eastern to recover costs expended to defend against allegations in state or private third-party complaints which are, in large part, identical to allegations in the EPA Complaint, when I have prevented Texas Eastern from recovering its defense costs in the EPA action. As such, F & C has no duty to defend against any of the claims presently included in this litigation.

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[111](...continued)
the duty to defend, an insurer is free to litigate the issue of coverage for the settlement. *See Employers Casualty Co. v. Block*, 744 S.W.2d 940, 943 (Tex. 1988). Moreover, Texas Eastern's reliance on *Rhodes* for the proposition that F & C must pay all damages assessed, including those not covered by the policies, is unavailing. *See Rhodes*, 719 F.2d at 120 n.5. As the Fifth Circuit recently observed, "[h]opeful insureds under Texas law cite this footnote [*Rhodes*, 719 F.2d at 120 n.5] in vain. . . . The insured does not win [unlimited] indemnification merely by showing that the insurer did owe it a defense in the underlying cause of action. Even an unfaithful insurer may not be bound to an insurance contract it did not write." *Enserch Corp. v. Shand Morahan & Co., Inc.*, 952 F.2d 1485, 1493 n.13 (5th Cir. 1992).

An appropriate order follows.

Donald W. VanArtsdalen, S.J.

July 9, 1992

ORDER AND FINAL JUDGMENT[1/]

For the reasons set forth in the accompanying opinion, it is hereby ORDERED that:

1. The Carriers' motion to strike is GRANTED IN PART AND DENIED IN PART—Exhibits eight (8) through eighteen (18) in the Declaration of Laird Hart and Texas Eastern Transmission Corporation's (Texas Eastern) "Statement of General Background Facts" are stricken. All

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1/ It has come to my attention that Southern American Insurance Company (one of the many London Market Insurers) is currently undergoing Liquidation proceedings. On March 26, 1992, Judge Anne M. Stirba of the Third Judicial District in and for Salt Lake County, State of Utah ordered that "[n]o suit, action, proceeding, or claim at law or in equity of any kind shall be brought, maintained, or further prosecuted [against Southern American Insurance Company] without proper authorization of the Liquidator . . . ." The Liquidator is Utah Insurance Commissioner Harold C. Yancey. Therefore, neither this order nor the accompanying opinion apply to Southern American Insurance Company.

I have also been informed that the following insurance companies: Kingscroft Insurance Company Ltd. (formally known as Dart Insurance Company Ltd., Kraft Insurance Company Ltd., and Dart & Kraft Insurance Company Ltd.), El Paso Insurance Company Ltd., Lime Street Insurance Company Ltd. (formally known as Louisville Insurance Company Ltd.), and Mutual Reinsurance Company Ltd. (collectively known as the "KELM Companies") are currently under a Temporary Restraining Order, dated May 8, 1992, entered by the United States Bankruptcy Court for the Southern District of New York, which prohibits "commencing or continuing any judicial, administrative or regulatory action or proceeding against Kingscroft, El Paso, Lime Street and/or Mutual or any of their property in the United States . . . ." Sherman & Sterling has informed the court that at least one of the KELM Companies is a party to the present litigation. Therefore, neither this order nor the accompanying opinion apply to the any of the KELM Companies which are parties to this litigation.

other evidence offered by any party to this litigation remains part of the official record;

2. The Carriers' supplemental motion to strike is DENIED;

3. The Carriers' motion for summary judgment on the "Occurrence" issue is DENIED;

4. The Parties' cross-motions for summary judgment on the issue of "Damages" are GRANTED IN PART AND DENIED IN PART. Losses incurred due to an injunctive order are compensable as "damages" under Texas Eastern's insurance policies. Civil penalties assessed by the United States Environmental Protection Agency are compensable as "damages" under Texas Eastern's insurance policies (excepting those policies which expressly exclude coverage for civil fines or penalties). Civil penalties assessed by the Pennsylvania Department of Environmental Resources and the New Jersey Department of Environmental Protection are not compensable as "damages" under Texas Eastern's insurance policies. In all other respects, the cross-motions are DENIED;

5. The Parties' cross-motions for summary judgment on the issue of the "Owned Property Exclusion" are DENIED.

6. The Carriers' motion for summary judgment on the issue of the "Pollution Exclusion" is GRANTED. No coverage will be provided for losses incurred by Texas Eastern under insurance policies containing either an ISO or London Market type pollution exclusion clause. Judgment in favor of all the Carriers whose insurance policies contain either of the two pollution exclusions and against Texas Eastern is entered on this issue;

7. Texas Eastern's motion for summary judgment on the issue of the "Pollution Exclusion" is DENIED;

8. The Carriers' motion for summary judgment on the issue of "Late Notice" is GRANTED. No insurance coverage is available for any of Texas Eastern's losses under any of its CGL insurance policies identified in this litigation, whether primary, excess, or umbrella policies, because Texas Eastern failed to provide the Carriers with timely notice of the claims for which it seeks insurance coverage. Judgment is entered in favor of all the Carriers and against Texas Eastern on the "Late Notice" issue;

9. Texas Eastern's motion for summary judgment on the issue of the "Duty to Defend" is DENIED. Fidelity & Casualty Company of New York (Fidelity) has no duty to defend Texas Eastern in any of the claims involved in this litigation. Judgment is entered in favor of Fidelity and against Texas Eastern on the "Duty to Defend" issue.

It is further ORDERED that, because I have concluded that Texas Eastern provided the Carriers with late notice of all the claims for which Texas Eastern seeks insurance coverage, final judgment is entered in favor of all the Carriers and against Texas Eastern. All remaining outstanding motions in " Texas Eastern Transmission Corporation PCB Contamination Insurance Coverage Litigation," MDL Docket No. 764, that are not determined

by this order are hereby DENIED as moot due to the entry of final judgment on all claims in favor of all insurance carriers.

BY THE COURT:

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Donald W. VanArtsdalen,

S.J.

July 9, 1992

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

- - -

IN RE:	:	MDL 764
	:	
TEXAS EASTERN TRANSMISSION	:	Philadelphia, PA
CORP. CONTAMINATION	:	September 15, 1988
INSURANCE COVERAGE	:	
LITIGATION	:	

- - -

BEFORE THE
HONORABLE DONALD W. VANARTSDALEN, J.
UNITED STATES DISTRICT JUDGE

- - -

THE COURT: Good afternoon, ladies and gentlemen. As I told you, I intend to state my decisions in these cases and I'll explain my reasons in general, although I don't intend to go into great detail or cite a lot of cases. Obviously, to the extent that I grant or deny a particular application, it would be primarily that I agreed with the briefs that have been submitted consistent with the decision that I reach.

I would like to make a certain preliminary statement as to the status of the cases so that that will be a matter of record here. The litigation involved in Multidistrict Litigation Docket 764 seeks by way of declaratory judgments a judicial determination of the respective duties and liabilities of approximately 23 insurers, to defend and indemnify Texas Eastern Transmission Corporation (Texas

Eastern) against claims for damages and costs of cleanup caused by Texas Eastern's discharging polychlorinated biphenyls, PCB's, at various locations along or near its natural gas pipeline system. It extends through 16 states from the natural gas fields of Texas to New York City or the vicinity of New York City.

PCBs' came under Federal regulation upon passage of the Toxic Substances Control Act, 15 USC Section 2601, et cetera, Texas Eastern and the Environmental Protection Agency, that is the EPA, have apparently reached an agreement, at least in principle, subject to approval of a consent decree that is presently pending, I believe, before another District Court, as to a cleanup program.

Texas Eastern estimates that this program will cost approximately $400 million, although that may include other possible contingent liabilities arising out of these PCB discharges.

In addition, several states including New Jersey, Kentucky and Pennsylvania, have asserted claims or the intention to file claims for damages and statutory, and other penalties and/or other legal proceedings against Texas Eastern by reason of alleged PCB contamination may be filed or have been asserted. Other actions may also be filed by various state and governmental agencies, private corporations and other legal entities and perhaps even individual persons.

From 1948 until the present, Texas Eastern was insured under various comprehensive general liability insurance policies. The policies varied as to the insurers, amounts of coverage, time periods of coverage and insuring clauses.

According to Texas Eastern, during the entire period of time Fidelity & Casualty Company of New York, which I'll call F & C from here on, was a primary carrier. 22 other insurance companies named as parties to one or more of the cases involved in MDL 764 were excess carriers in various amounts and during various periods of time, and some of the 22 insurance companies may also have been primary carriers during certain periods of time.

All parties to this litigation apparently agree that all issues of insurance coverage should, if possible, be finally determined in a single form and that he disputes should all be resolved in a consolidated proceeding and not be fragmented into discrete lawsuits filed in various courts.

The dispute among the parties at this stage of the proceeding is the appropriate forum in which to have the matters resolved. In the present posture of the cases, Texas Eastern contends that the only proper forum is in the Texas State Courts and that all litigation should either be remanded to that forum or dismissed or stayed pending resolution of the issues through the Texas State Courts.

Texas Eastern contends that the issues do not involve matters of Federal law but solely matters of insurance contract interpretation under state and common law and that there is no basis for Federal diversity jurisdiction or any other basis for Federal jurisdiction. Texas Eastern therefore challenges the jurisdiction of this or any other Federal Court to decide the issues in the cases comprising MDL 764.

All of the other parties to this litigation appear to be of the view that the Federal Courts can and should decide the matters in dispute and, at this juncture, would at least not object to the actions being finally determined at the trial level in the Eastern District of Pennsylvania.

In theory, at least, if all the cases were resolved and all the issues resolved in one particular court or one particular forum, in theory, at least, the ultimate decision in the case should make no difference whether it is tried in Federal Court or in State Court or in what particular forum.

I recognize, of course, that there are practical problems that do not necessarily mean that there would be no advantage to one side or the other having the cases tried in State Court as opposed to Federal Court or in some particular court as opposed to this court.

To put the present procedural and jurisdictional problems in proper context, a brief chronological review of the various prior and pending actions would appear to be helpful.

The first action was filed by F & C against Texas Eastern. F & C and Texas Eastern were and are the only parties to that action, which was filed in the Northern District of Texas on December the 11th, 1987, and docketed in that court as CA3-87-2925-2.

A motion to dismiss or stay was filed by Texas Eastern by reason of a later filed pending action in New Jersey State Court brought by Texas Eastern against all of its insurers, including F & C. The motion to dismiss or stay was denied. A motion for reconsideration was also denied. However, it has been called to my attention that that was done or at least dated and filed after the Multidistrict Panel transferred the case to this district.

By order of the Judicial Panel on Multidistrict Litigation, or the Multidistrict Panel, dated May 31, 1988, the case was transferred pursuant to 28 USC Section 1407 to this district for coordinated and consolidated pretrial

proceedings, or Civil Action 88-2126 then pending in the Eastern District of Pennsylvania.

This case from Texas has been transferred, filed and docketed in this district as Civil Action 88-5039 and will hereafter be referred to as the F & C action.

On December 19th, 1987, Texas Eastern filed action against all of its alleged various insurers, including F & C, in State Court in New Jersey. The case was titled *Texas Eastern Transmission Corporation versus Fidelity & Casualty Company,* docketed as No. WO-30685-87 and filed in the Superior Court of New Jersey.

On motion of one or more of the defendants to dismiss on the grounds it formed nonconvenience, the motion was granted and the case was dismissed on March 17, 1988. This was the New Jersey State action that was the basis for Texas Eastern's motion to dismiss or stay the action then pending in the Northern District of Texas.

Texas Eastern took no appeal from the dismissal of the New Jersey State action.

On March 11, 1988, Associated Electric & Gas Services, Limited, (AEGIS), and National Surety Corporation filed action in this district, that is the Eastern District of Pennsylvania, against Texas Eastern, F & C, and all other insurance carriers, whether primary or excess carriers. The Complaint also named the United States of America and the United States Environmental Protection Agency as defendants.

Jurisdiction was asserted on the basis that one of the main defendant insurers, the Insurance Company of Ireland, which I will hereafter refer to as ICI, was a "foreign state,"

as defined in 28 USC Section 1603, and that 28 USC Section 1330 provides District Courts with original jurisdiction against such entities.

Jurisdiction was also asserted over the United States and the EPA pursuant to 28 USC Section 1346.

The Government defendants have moved to dismiss as to them for failure to state a claim against them and for lack of subject matter jurisdiction by reason of sovereign immunity.

Texas Eastern has moved to dismiss, or in the alternative, to stay the action, contending, A, that there is no cause of action against the United States and the EPA; B, that even if ICI comes within 28 USC Sections 1603 and 1330, its interests in the controversy are *de minimus* and it should be dismissed, thus ending Federal jurisdiction. And in any event, ICI as well as all of the other insurers, should be aligned as plaintiffs, thus again defeating jurisdiction under 28 USC Section 1330.

ICI, as well as plaintiffs and other insurance carriers, contend that ICI has a right to have the controversy determined in a Federal forum pursuant to 28 USC Section 1330 or, even if it were filed in State Court, to have it removed to Federal Court pursuant to 28 USC Section 1441A and contends, further, that ICI's interests are adverse to plaintiffs and it is therefore properly aligned as a defendant vis-a-vis the plaintiffs and that the monetary amount of its interest or stake in the controversy is irrelevant to the issue of this Court's subject matter jurisdiction under the Foreign Sovereign Immunities Act (FSIA), 28 USC Section 1602, et cetera. This action is docketed as Civil Action 88-2126 and will hereafter be referred to as the AEGIS action.

It was by reason of this action that the Multidistrict Panel transferred the F & C action to this court, or at least the action was pending in this court at the time that the F & C action was transferred to this court.

On March 21, 1988, four days after the dismissal of the New Jersey State Court action, and while the F & C action was pending in the Northern District of Texas and the AEGIS action was pending in this court, Texas Eastern in substance refiled its New Jersey State action against all of its insurers, including F & C and the plaintiffs in the AEGIS action, in the State Courts of Texas, being the 215th Judicial District of Texas, Harris County, Texas, where the case was docketed as 88-15573.

On June 3, 1988, ICI, an excess insurance carrier on several policies of insurance but not identified by its corporate name as a party defendant in the Complaint nor formally served as a defendant, although admittedly a party sought by Texas Eastern to be barred by any final judgment as one of the several named "Lloyd's" insurance defendants, removed the case to the Federal Courts, Southern District of Texas, Houston Division, where it was docketed as CA H-88-1910.

By order dated July 7, 1988, Honorable Lynn Hughes, District Judge, transferred the case to this district, presumably on the basis of 28 USC Section 1404(A).

A conditional transfer order by the Multidistrict Panel dated July 5, 1988, was vacated by order dated July 20, 1988, apparently because of Judge Hughes' prior transfer order.

Prior to transfer to this district, Texas Eastern filed a motion to remand the case to the Harris County State Court,

contending that, A, the removal by ICI was untimely; B, ICI had contractually waived the right to remove; and, C, that substantively ICI under the established facts was not entitled to removal as a foreign state-owned corporation under FSIA.

This action has been docketed in this court as Civil Action 88-5707 and will hereafter be referred to as the Texas Eastern action.

There are, therefore, now pending in this court, whether rightly or wrongly, three actions, namely, the AEGIS Civil Action 88-2126, the F & C Civil Action 88-5039 and Texas Eastern Civil action 88-5707.

All three actions seek declaratory judgment as to the rights, duties and liabilities among the parties in respect to insurance coverage for the PCB contamination by Texas Eastern.

There are presently no other pending actions of which I am aware involving the same subject matter and, so far as is known, no other actions are contemplated.

Texas Eastern, seeking to have the case litigated in State Courts, in the State Courts of Texas, challenges jurisdiction asserted in the AEGIS action and challenges the right of ICI to remove the Texas Eastern case from the Texas State Courts to the Federal Courts.

Although I do not understand Texas Eastern to challenge jurisdiction in the F & C action, it continues to seek a dismissal or stay by reason of the other pending actions.

As to the motion to dismiss or stay in the F & C action, as I see it there is no pending motion before this Court. The motion was denied by the District Court of the Northern District of Texas and that decision was reaffirmed admittedly after transfer on the denial of the motion for reconsideration.

To the extent, however, that there may still be an issue of the motion for reconsideration which I would have the right to dispose of, I would agree with the determination of the Northern District of Texas that the motion for reconsideration should be denied.

It seems to me, in addition, that the determination by the Northern District of Texas, the decision is the law of the case and that there were no changed circumstances that would justify any different decision.

I would agree, however, that if there were changed circumstances by reason of the transfer of the Texas Eastern action to this district or by reason of some disposition that may be made as to the pending motions, a reapplication to dismiss or stay would not necessarily be foreclosed. It is clear, however, that the F & C action was properly filed in Federal Court in the Northern District of Texas and was properly transferred by the Multidistrict Panel to this Court.

Diversity jurisdiction in that case was properly alleged and is not challenged. The action involves only the rights, duties and liabilities existing between F & C, the primary insurer during the entire relevant time periods in issue, and the insured, Texas Eastern.

A final judgment in the F & C action would, of course, not bind other insurers not parties to that action. As a practical matter, however, a final judgment in the F & C

case would probably decide most of the principal issues that will have to be addressed in the other actions involving the rights, duties and liabilities of the excess insurance carriers and might moot many of the other issues that will be presented in the AEGIS and Texas Eastern actions.

A final judgment in the F & C case to the extent, if any, that it would be favorable to the insured F & C, would probably operate against Texas Eastern in any of the other actions involving excess insurance carriers through the Doctrine of Collateral Estoppel.

In any event, to the extent that Texas Eastern continues to contend that the F & C action should be dismissed or stayed, I will not at this stage of the proceedings enter an order dismissing or staying the F & C action, 88-5039, irrespective of whether I would have the right to enter such an order in light of the rulings heretofore made by the transferor court denying the motion, and thereafter the transfer by the Multidistrict Panel to this Court.

The Texas Eastern action, 88-5707, is in a different posture than 88-5039 because 88-5707 was transferred as a change of venue and consequently obligates this Court to bring the case to a final conclusion, provided there is proper jurisdiction.

Texas Eastern's cause of action as filed in the Harris County Texas State Court alleges only state and common law causes of action. No Federal cause of action was asserted or appears from the Complaint.

Clearly the Texas State Court, assuming it did or could acquire a valid personal jurisdiction over all of the parties as to which there appears to be no dispute had subject matter jurisdiction to decide the case on the merits.

ICI chose to remove the case to Federal Court, allegedly pursuant to the right granted it by Federal statutes. If under those statutes ICI had the right and the option to remove the case to Federal Court, such removal would operate to remove the entire case and all of the parties, irrespective of the preference of the parties to remain in State Court.

I do not believe that any party to MDL 764 contends to the contrary; at least there are none so far as I am aware. Clearly also if the case was properly removed to Federal District Court in Texas, that Court had the right to transfer under 28 USC Section 404(A) to any other district where this action might have been brought.

If there is a proper basis for Federal jurisdiction, I do not think that any litigant disputes that the action might have been brought in the Eastern District of Pennsylvania. Conversely, if ICI improperly removed the case to Federal Court, then Texas Eastern's pending motion to remand to Harris County Texas State Court, which motion was filed prior to the transfer and left undecided, would seemingly, at least, have to be granted.

A rather extensive argument of Texas Eastern that ICI's interest in the case is *de minimus* and therefore ICI should be precluded from removing the case from State to Federal Courts is totally unavailing. If ICI is a "foreign state" within the statutory definition, it has the right to remove the case to Federal Court irrespective of its monetary interest or stake in the matter, and that is expressly so provided by statute, provided of course that it has some justiciable issue to be decided. Although ICI was not identified by name as a defendant, Texas Eastern does not dispute that ICI is in fact one of many excess carriers and that ICI should be bound by whatever decision is finally rendered in this case.

Rather at least as to the timeliness of the removal petition, Texas Eastern contends that ICI knew all along that it was in fact a defendant. A Federal Court does not have the right to decline jurisdiction where its jurisdiction is properly established nor may a Federal Court remand to a State Court a case properly removed from a State Court on any equitable grounds or as a discretionary matter, even though the State Court may have concurrent jurisdiction.

Finally, as to Texas Eastern's *de minimus* argument, there have been submissions made which if properly authenticated and proved establish beyond question that ICI has a potential liability as an excess insurer of at least several million dollars.

If I may digress for a moment, even in these days of multibillion dollar annual Federal deficits, several million dollars to a private corporation hardly constitutes a *de minimus* amount in controversy. As a former statesman or politician, depending on one's point of view, reputedly state in effect some years ago that a few million dollars here and a few million dollars there and pretty soon, you know, we're talking about a lot of real money.

The only remaining issues to be decided as to the Texas Eastern action, therefore, are, one, whether ICI is a foreign state within the meaning of FSIA and, two, if so, whether it timely removed the case to Federal Court and, three, whether it contractually waived its right to remove.

As will be discussed later, I conclude that the case was properly removed to Federal Court and therefore the remand to State Court will not be granted.

In the AEGIS Civil Action 88-2126, jurisdiction is founded on 28 USC Section 1346 because the United States

and the EPA are defendants and 28 USC Section 1330 by reason of ICI being alleged to be a foreign state as defined in 28 USC Section 1603(A) under FSIA, Texas Eastern contends that ICI is not a foreign state within the definition of 28 USC Section 1603(A) and, even if it is, it must be realigned as a plaintiff and as such neither the AEGIS plaintiff nor ICI would have the right to have the case decided in a Federal forum.

Obviously, as to many of the issues, the interests of all of the insurance companies will be aligned against the interests of the insured, Texas Eastern, the same as the interests of the insurers as to the present motions appear to be in harmony and are opposed by those of Texas Eastern.

However, in the event that it is determined that any insurer is liable to defend or indemnify Texas Eastern for any period of time, for any amount or as to any type of liability, the position of the other insurers will of necessity be diverse and adversarial toward each other.

The matter of insurance coverage as to all parties is sought to be adjudicated in the AEGIS action as well as the Texas Eastern action. The AEGIS plaintiffs have the right to seek a declaratory judgment vis-a-vis Texas Eastern and also vis-a-vis each and all other insurers, whether primary or excess insurers.

Two or more of the insurers may have a common interest in escaping all liability, but that does not mean that their interests are harmonious. As was stated in *American Motorist Insurance Company vs. Trane Company,* 657 F. 2nd 146, Seventh Circuit 1981, in which they held in effect that the District Court realigning insurers as plaintiffs and thus defeating the purpose of the jurisdiction was error in the District Court.

I reached similar conclusions in *Evanston Insurance Company vs. PPG Industries, Incorporated,* Civil Action 85-4179, an unreported case, and recently in *United States Fidelity & Guaranty Company vs. The Kormann Corporation,* which will be reported in _____ Fed Supplement _____, Eastern District of Pennsylvania 1988. Cases that I decide may or may not be persuasive precedent, but at least I like to be, wherever possible, consistent with prior opinions that I have rendered unless they have been otherwise found to be in error by a Court of Appeals or the Supreme Court.

Consistent with those opinions I conclude that the plaintiffs and the defendants are properly aligned in the AEGIS action for purposes of determining jurisdiction. Thus, there is a natural controversy between plaintiffs and ICI. 28 USC Section 1330(A) provides that the District Court shall have original jurisdiction without regard to the amount in controversy of any nonjury civil action against a foreign state as defined in Section 1603(A) as to any claim for relief *in personam* with respect to which the foreign state is not entitled to immunity either under Section 1605-1607 or under any other applicable international agreement.

28 USC Section 1603(A) defines a foreign state to include "An agency or instrumentality of a foreign state," which is further defined in Subsection B as an entity which is a separate legal person, corporation or otherwise, a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof and by interpolation is not a corporate citizen of the United States or created under the laws of a third country.

The Complaint alleges, Paragraph 11, that the defendant, ICI, is a separate legal person, a corporation or

other business entity a majority of whose shares or other ownership interest is owned by the Republic of Ireland, that because of the commercial activity within this country carried on by ICI, namely insurance, ICI is not immune from suit and that there is no international agreement affording it immunity, and therefore under 28 USC Section 1330(A) that this Court has original jurisdiction.

There is some dispute between Texas Eastern and ICI as to whether ICI comes within the protection of FSIA. The Complaint in the AEGIS action makes a sufficient allegation that ICI is a foreign corporation whose stock is wholly owned by the Republic of Ireland.

There may be some question as to who has the burden of proof on the issue, but ordinarily it would appear to be the party asserting Federal jurisdiction. In the Texas Eastern case, clearly the burden would be on ICI because it is the removing party.

In any event, ICI submitted in the Texas Eastern case an affidavit of J. G. Banks, the Chief Executive Officer of the Insurance Company of Ireland. The affidavit sets forth that ICI is a corporation organized and existing under the laws of the Republic of Ireland, that in March 1985 the Government of Ireland acquired 100 percent shares of ICI through a wholly owned corporation and since March 1985, ICI has been operated by an Administrator appointed by the Government.

In opposition to the Banks affidavit, there is a declaration by David W. Prentice, an Irish solicitor. His declaration sets forth that "Virtually all of ICI's capital was transferred to" — and I will spell this and not try to pronounce it — S-E-A-L-A-C-H-A-I-S, first word, second word A-R-C-H-A-I-S, third word T-E-O-R-A-N-T-A, which

I will hereafter refer to as SAT, "a limited liability company, and that SAT continues to hold all of ICI's shares, that ICI has been under the administration of the High Court entered pursuant to the Statutes of Ireland since March 25th, 1985." Although it is alleged in the affidavit or declaration that the administration is similar to a Chapter 11 proceeding under United States Bankruptcy laws, it is also averred that the administrator is entitled to the powers of management and shareholder.

There was a subsequent affidavit filed by Mr. Banks together with, and there were attached the statutes of Ireland that were applicable in this case, and also attached a copy of a court order. It makes it clear to me that in return for the Ministry of Industry and Commerce of Ireland guaranteeing certain debts of ICI, which I believe was to the extent of 20 million pounds, all of the shares of SAT and hence of ICI were transferred to the Minister of Industry and Commerce and that the sole shareholders and directors of SAT have been two officials of the Department of Industry and Commerce.

Another Irish statute, which I believe is in Insurance Miscellaneous Provisions, No. 8, of 1985, provided for the Minister of Industry and Commerce to acquire all of the shares of SAT, to provide for the guarantee of the 20 million pounds of debts to the insurance, of the Insurance Corporation of Ireland.

The Minister was also authorized to hold and sell any and all shares of SAT and may exercise all of the rights and powers of holders of shares and receive all of the dividends, any dividends that were to have been received or profits were to go to the Exchequer of Ireland.

Thus it seems clear that although ICI may be under the administration of the Courts for some purposes, a majority of the shares of ICI, "or other ownership interests" is owned by the Republic of Ireland. The statute provides that it be a majority of the shares or other ownership interest. Since SAT owns 100 percent of ICI's shares and SAT is 100 percent owned and controlled by the Republic of Ireland through its Minister of Industry and Commerce, and the sole shareholders and directors of SAT are officials of the Department of Industry and Commerce, there is a direct and complete ownership of ICI by the Republic of Ireland for purposes of 28 USC Section 1603.

That being so, there is no doubt that AEGIS, by naming ICI, properly filed this action in Federal Court. That action, therefore, cannot be dismissed.

Although AEGIS also contends that Federal jurisdiction is proper because it named as defendants the United States of America and the EPA, the governmental agencies have moved for dismissal.

It is clear that the Government and the EPA are in no way involved in the present controversy as to whether Texas Eastern has insurance coverage for the whole or any part of the losses or costs Texas Eastern may incur as a result of Texas Eastern's discharge of PCBs' or by reason of any litigation or settlement of claims by the Government or the EPA.

Although counsel for AEGIS points out that it is not inconceivable that if the insurance companies are held in these cases to be liable to Texas Eastern that the Government at some point might attempt to bring a suit directly against the insurance carriers to recover for any claims or losses that Texas Eastern is unable to cover.

That, however, is not a present controversy. In addition, even if it were a present live controversy, the United States, as the sovereign, is immune from suit. And although it's been suggested that the immunity only extends if there is something sought by way of money damage or an injunction against the Government, I think that it is quite clear that absent some statutory basis for bringing suit against the Government or the EPA, under these circumstances that the sovereign immunity applies and that there cannot be a suit against the United States of America or the EPA. And therefore the motion will be granted as to the dismissal of the United States of America and the EPA.

Although I have concluded that the AEGIS case is properly filed in this court and cannot be dismissed, it is possible that I would have the discretionary power and right to stay both the AEGIS and the F & C actions in the event the Texas Eastern case is remanded back to the Texas State Courts.

The case of Texas Eastern can be remanded to the State Courts only if it was improperly removed. I have already decided, as heretofore noted, that ICI is a corporation that comes within the provisions of FSIA. As such, when sued in State Court, it clearly had the right to elect to remove the case to Federal Court.

28 USC Section 1441(D) provides that any action filed in a State Court against a foreign state as defined in Section 1603(A) of this title may be removed by a foreign state to the Federal District Court. As previously noted, I conclude that ICI is a foreign state as defined in 28 USC Section 1603(A). Therefore, it had the right to remove to the District Court of Texas.

Nevertheless, Texas Eastern contends that, one, ICI by contract waived the right to remove the case to Federal Court and, two, the removal was untimely.

Considering first the timeliness of the removal, 28 USC Section 1446(B) provides that a petition for removal shall be filed within 30 days "after receipt by the defendant, through service or otherwise, of a copy of the initial pleadings setting forth the claim for relief upon which such action or proceeding is based or within 30 days of service of summons."

This time limit has frequently been held to be jurisdictional and non-waivable. Texas Eastern contends that ICI did not file the removal petition until 63 days after it was served. It should be noted, however, that even to this day, ICI is not named or identified in the pleading as a defendant in its corporate name, as such, nor was it ever served in this corporate name.

ICI contends that it did not know until May 23rd, 1988, that it was in fact being sued and the petition to remove was filed on June 3rd, 1988. ICI was apparently intended to be included as one of the "Lloyd's Companies," as a defendant, and service was made upon Lloyd's local agent, Mendis & Mount.

Texas Eastern also claims that ICI knew it was being sued because a meeting was held between Texas Eastern and all of its insurers prior to, I believe, any of the suits being filed. This, however, would not meet the requirements of Section 1446(B), a receipt of a copy of the initial pleading or service of a summons.

Were this issue critical to my decision, which it is not, I would include that ICI did timely file the petition to

remove, that the 30-day period for purposes of 28 USC Section 1441(B) has never to this day commenced to run.

In any event, 28 USC Section 1441(D) expressly provides that the time limitations of 1446(B) may be enlarged at any time for cause shown where suit is against a foreign state. Because Congress has expressly provided that foreign states may have non-immune cases against them tried in Federal Court and this it seems to me is a matter of public policy involving international relations, the statute should be construed in favor of allowing removal to Federal Court. I can see no prejudice to Texas Eastern or any equities in favor of Texas Eastern in not permitting the removal.

Again, I point out that the issue is not a substantive issue, it's merely an issue as to what court or what forum the matter should be litigated. In this case, it seems to me clearly not only has good cause been shown to extend the 30-day period if that was required, it seems to me that there is good cause to enlarge the time if enlargement is necessary.

I say this because certainly until Texas Eastern, by later filings, made it expressly clear that ICI was sought to be held liable and bound by any judgment, it was at least open to argument that ICI was a party. Certainly ICI had no obligation to voluntarily make itself a party by unnecessarily seeking removal. Clearly I see no way that any binding judgment by default could have been entered against ICI had it done nothing.

However, since all parties now agree that ICI is or at least should be a party, to the extent if any the removal petition would not have been timely under 1446(B), the time limitations I will enlarge. And I would note that so far as I

can tell by the statute, they may be enlarged at any time. Presumably, therefore, they may be enlarged without prior motion or approval and could be done *sua* sponte.

A final argument has been made that ICI has by contract "waived" the right to remove the case to Federal Court. The insurance policies as to which ICI subscribed a proportionate part contain clauses that the insurers at the request of the insured would submit to the jurisdiction of any court of competent jurisdiction within the United States and would comply with all requirements necessary to give such court jurisdiction.

Similar so-called service of suit clauses have been held by a long line of cases to constitute a waiver of the right to remove a case from State Court. Logically, it seems to me, and if I were writing on a clean slate without any prior case law in this regard, it would seem to me that ICI has not challenged the jurisdiction of the State Courts of Texas. It did in fact submit to the jurisdiction of the Texas State Court, but then proceeded in accordance with provisions of Federal statutes to remove the case to Federal Court. And we all know that even a case that is removed to Federal Court, must be dismissed if the State Court did not have original jurisdiction in the matter, at least in diversity cases.

Nevertheless, I recognize that most cases have held to the contrary. For instance, *Cessna Aircraft vs. Fidelity & Casualty Company of New York,* 616 Fed. Supplement 671, District Court, New Jersey, 1985.

In the present case, however, the removal is based on FSIA. In *Proyecfin de Venezuela, S.A. vs. Banco Industrial de Venezuela,* that's spelled P-R-O-Y-E-C-F-I-N D-E and Venezuela, S.A. versus Banco, B-A-N-C-O, Industrial de Venezuela, 760 F. 2nd 390, 2nd Circuit, 1985, the Second

Circuit concluded that a form selection clause, at least where the selection clause merely accedes to jurisdiction in either Federal or State Court, which is of the same effect as the present clause, does not preclude removal to Federal Court by a defendant qualifying as a foreign state or corporation owned by a foreign state.

Wright, Miller & Cooper, Federal Practice & Procedure, Section 3729, Page 486, I believe, opines that, "It is likely that a Federal Court would accept removal jurisdiction of an action against a foreign state even in the face of an express waiver."

Congress has made clear by enacting FSIA that foreign states and instrumentalities of foreign states such as foreign state owned corporations shall have the right to have civil litigation decided in Federal Court. Certainly a clause that merely agrees that such a corporation will submit to the jurisdiction of any competent court is not an express waiver, even if it is a matter that may be waived by contract.

Finally, Texas Eastern argues that the right of removal is dependent upon the time the contract of insurance was executed and as of that time, ICI was a wholly private corporation. I disagree with that argument.

The right to remove depends on the facts, as I see it, that exist at the time the petition to remove is filed. *In Re Carter,* 618 F. 2nd, 1093, Fifth Circuit 1980, I believe supports that position. In any event, it would seem to me certainly it would be when the cause of action arises and this declaratory action is for nonperformance of the contract and at least as of that time, ICI was wholly owned by the Republic of Ireland.

I think, also, the comparison with or the analogy with removal and diversity cases, clearly there the diversity must exist as of the time of the removal as an analogous situation to the right to remove under FSIA insofar as the time at which the government ownership must appear.

My final conclusion as to the Texas Eastern case is therefore that removal by ICI was proper, that is, that it was timely, it was by an instrumentality of a foreign state, and that ICI did not waive the right to remove on the basis of FSIA. The case having been properly removed, it cannot be remanded to State Court.

My decision that ICI may properly have its litigation determined in Federal Court is reinforced by a recent decision by Judge Mencer of the Western District of Pennsylvania in the case of *Liberty Mutual Insurance Company vs. The Insurance Corporation of Ireland, Ltd., et al.,* which was Civil Action 87-1901, the opinion rendered August 30, 1988, and will be reported in Blank Fed. Supp. Blank, Western District of Pennsylvania, 1988.

The *Liberty Mutual* case decides as similarly I decide many of the issues that are applicable in this case. The *Liberty Mutual* case was filed in Federal District Court by the primary insurer against its insured and all of the other secondary insurers seeking declaratory relief.

Also similar to the present action, Liberty Mutual filed the action after the New Jersey State Courts dismissed most of the issues involved upon an action by the insured, Westinghouse, against its insurers. Also the case involved toxic waste claims against Westinghouse, some of which were brought by the EPA and involved claims in at least 23 states, approximately 130 insurers and a time span of many years.

The basis for Federal jurisdiction in the *Liberty Mutual* case, like that of the AEGIS and also the Texas Eastern removal action, was that ICI was a named defendant and the contention that it had the right to be in Federal Court under FSIA.

Westinghouse, in that case, moved to dismiss for lack of Federal jurisdiction. Now, the only differences, though there are several differences in that case from this case, in the case before Judge Mencer Liberty Mutual was the primary insurer and Westinghouse did not contest that the shares of ICI were, in fact, owned by the Republic of Ireland. But it pointed out, I think, the evidence that has been submitted makes it clear beyond any question that ICI does come within the terms of a corporation wholly owned by a foreign state.

I see no reason why there would be any difference whether the suit was brought by a primary insurer or by a secondary or any one or more of the other insurers.

In the *Liberty Mutual* case the issue of party alignment was also raised. Judge Mencer ruled that for purposes of deciding if the case was against ICI, it was properly a defendant and, as such, the Federal Court had original jurisdiction. And he also held that that jurisdiction extended over all other defendants and the entire controversy.

He also determined that there would, in any event, be dependent party jurisdiction over the other defendants, an issue which I expressly will not decide as it is unnecessary to decide in this case, as I see it.

Where the case is removed, and certainly as to the Texas Eastern case, where the case is removed under FSIA as in the Texas Eastern case, there are cases that establish

that that removes the entire action and all parties. And it would seem there should be no logical reason why it would make any difference whether the case got into Federal Court through removal by the foreign state or foreign state owned corporation, or whether it got into Federal Court by reason of it being originally filed there against the foreign state or foreign corporation.

I agree with Judge Mencer's decision insofar as it is applicable to the facts of the present litigation. And therefore, I will enter the following order.

It is ordered that in MDL 764, as follows:

One, Civil Action 88-2126 "AEGIS action," the motion of the defendant, Texas Eastern Transmission Corporation, to dismiss or stay the action is denied.

The motion of the defendants, the United States of America and the United States Environmental Protection Agency, to dismiss the Complaint as to those defendants is granted.

Two, in Civil Action 88-5039, the "F & C action," the motion of the defendant, Texas Eastern Transmission Corporation, to dismiss or stay the action and/or for reconsideration of the orders of the District Court of the Northern District of Texas, Dallas Division, denying said motion are denied.

Three, in Civil Action 88-5707, the "Texas Eastern action," the motion of the plaintiff to remand the action to the State Courts of Texas, namely the District Court of Harris County, Texas, 215th Judicial District, is denied.

And I will enter a formal written order to that effect, hopefully, today.

Now, ladies and gentlemen, I believe that that covers all of the issues and motions presently pending before me. I know that I said that you did not all have to be here this afternoon; I see that most of you are here. And I would like, and I forgot to mention this this morning, and also because I did not want to let it be known what my probable decision would be, although I considered it further over the noon hour, as to what procedure should be followed from this point on.

We have of course the three actions: 88-2126, 88-5707 and 88-5039. And, incidentally, gentlemen, hereafter when you make filings in this court, will you please use those correct numbers because I quite frankly had a lot of difficulty. I had some that had the 1910. I'm not criticizing any counsel for that but I think it would be easier if we did it that way where it's necessary to identify a particular case, rather than the MDL 764.

I will of course be open to suggestions. It would appear to me that perhaps the parties might be able to agree by stipulation without waiving any appellate rights that they might presently or hereafter have as to any rulings, that we should proceed to trial on, I would suggest, the AEGIS case. I don't know that it really makes any difference whether it would proceed on that one or whether it would proceed on the other, but I would be open to suggestions of anybody as to that.

In any event, we should now proceed with discovery without delay and, of course, any discovery that is taken in any of these cases, whether they are technically consolidated or not, and I think where they're under multidistrict

litigation they are consolidated as a matter of law in any event. But to the extent that they are not, in any event, any discovery taken in any of these cases shall be considered as discovery in all cases.

And does anyone have any thought as to how long, how extensive discovery is going to be? This is a case, basically, when it gets down to the final issues it seems to me will probably be practically entirely matters of law. I understand that the facts may be very complicated as to who covered what, when and where, why maybe, but. . .

MR. MESERVE: I think that there might be a lot of factual background about who knew what, when.

THE COURT: There may be, may be.

MR. L. RIVKIN: May I mention to the Court —

THE COURT: Yes.

MR. L. RIVKIN: — something I mentioned earlier. I don't know whether you'd care to hear it now, but would you care to consider that consolidation motion just to clear the record up on that one case that's not part of MDL so that they would be —

THE COURT: Yes, that's true technically, that should be done.

MR. L. RIVKIN: May I so move if there's no opposition?

THE COURT: Well, I don't know whether there would be or not, but —

MR. MESERVE: Your Honor, we're in a situation where I know many of the defendants in the case are not present.

THE COURT: I think it should be done by a formal motion.

MR. L. RIVKIN: Sure, I have no problem. I withdraw the request.

THE COURT: Okay. I'll leave it up to counsel, though, to make suggestions as to how or whether we can proceed on one particular case. As I said, the AEGIS case is in this court. I would have the right to proceed with it, irrespective of the Multidistrict Panel litigation matter and it seems to me that it will cover all issues, except as you mentioned, there may possibly be one additional claim in the F & C case. I think somebody mentioned that.

Does anybody have any suggestion or would counsel like to confer and perhaps see if they can get together on a proposed discovery order and submit it to the Court?

MR. MESERVE: Your Honor, I believe at the last status conference we had discussed very briefly the prospect that counsel would try to work together and develop a proposed scheduling order for the case. That has been deferred, I think, in large part because the forum was uncertain. I am sure that we would welcome the opportunity to see if we can work something out and we could be prepared to do that and then submit something, hopefully, jointly for your consideration.

THE COURT: All right.

Yes, Mr. Carr?

MR. CARR: Your Honor, I'm Lawrence Carr.

We had been considering the case management plan which had been circulated to the defense at this time for their consideration, but pending the decision today we haven't gone any further on that. I would suggest that before we gather with the plaintiffs, I guess they're the plaintiffs at this time, that we go forward and firm up own ideas about this plan and then present them and meet the plaintiff's counsel and see if we can work out something to present to the Court in a relatively short period of time.

THE COURT: All right. Now, how much time do you want? Because it's important that we not just let the thing hang free in case you're unable to reach an agreement or something of that sort, then it may require some intervention on my part.

MR. CARR: Speaking for myself alone, I would think that two weeks would be adequate for us to accomplish this. I may be overly optimistic, but that's my thinking in it.

MR. MESERVE: Your Honor would not, of course, be privy to what the insuree is suggesting. It's very difficult for us to be able to comment today as to how long it would take to resolve any differences that may exist. I would think given the large number of defendants and so forth that two weeks is likely to be optimistic.

MS. D'AMATO: Your Honor, I think that two weeks would be adequate for the defendants to be in a position to submit something to Texas Eastern and then perhaps another two weeks after that to put together a joint proposal.

THE COURT: Yes, I think so. I find no matter what time limits I put on those, the attorneys generally don't do much until two days before the time limit is up.

(Laughter.)

THE COURT: All right. Where are we now?

Well, we'll give you until the 14th of October. That's a month from now. If you haven't been able to reach agreement at that time, at least I would want a status report, letter from all antagonistic views or different views on the matter, as to what issues have to be decided and then we would proceed from there.

All right. Anything further that we can do at this time, ladies and gentlemen?

(No response.)

THE COURT: All right. Thank you very much.

And I thank everybody, the briefs certainly were excellent and I think covered everything that could be covered.

(Proceedings adjourned at 2:35 p.m.)

* * *

CERTIFICATION

I hereby certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

_____ _____

Geraldine C. Laws Date
Laws Transcription Service

_____

Mary Morrow

_____

Grace Williams

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

ALUMINUM COMPANY OF AMERICA, et al.,	)	
	)	
Plaintiffs,	)	CASE NO. C93-32C
	)	
v.	)	MINUTE ORDER
	)	
ADMIRAL INSURANCE COMPANY, et al.,	)	
	)	
Defendants.	)	
	)	

The following Minute Order is made by direction of the Court, the Honorable John C. Coughenour, United States District Judge:

This matter is before the Court on plaintiffs' motion to remand. Plaintiffs' request for oral argument is declined. After reviewing all relevant documents and being fully informed, the Court finds and rules as follows:

As an initial matter, the Court addresses whether Icarom had standing to remove this action even though it was not a defendant. The Court's reading of the removal statute, 28 U.S.C. § 1446 indicates that is does not. Specifically, § 1446(a) provides that "[a] defendant or defendants desiring to remove any civil action" must file a notice of removal. Moreover, § 1446(b), which sets the deadline for filing a notice of removal, refers only to "the defendant." Icarom cites no authority in support of its contention that an unnamed party has standing to remove an action to federal court. In sum, the Court concludes that Icarom lacked standing to file the notice of removal here.

Although the Court's finding that Icarom lacked standing to remove this action obviates the need to reach the merits of plaintiff's motion, the Court will discuss the merits in the interest of avoiding a similar sequence of events should Icarom be added as a defendant.

Stated succinctly, the doctrine of issue preclusion[1/] prevents relitigating issues of fact or law that have been litigated and decided in prior actions. *Robi v. Five Platters, Inc.*, 838 F.2d 318, 322 (9th Cir. 1988). To invoke the issue preclusion doctrine, the issue must have been "actually decided" after a "full and fair opportunity" for litigation. 18 Charles Wright, Arthur Miller & Edward Cooper, *Federal Practice & Procedure: Jurisdiction* § 4416, at 138 (1981).

The precise issue presented here—whether Icarom is a foreign state for FSIA purposes—is not novel, and has been directly addressed by several courts. Most recently, a federal district court in Arkansas specifically held that Icarom "is not a foreign state under the FSIA." *Murphy Oil USA, Inc.* v. *United States Fidelity & Guaranty Co., et al.*, No. 91-1157 (W.D. Ark. Dec. 21, 1992). The *Murphy Oil* Court relied heavily on, and incorporated by reference, a 1990 case from the Southern District of Texas. In that case, *Mobil Corp. v. Abeille General Ins. Co.*, No. H-89-3877 (S.D. Tex. Nov. 6, 1990), the court found that "the role of the Irish government in the affairs of [Icarom] does not constitute government ownership nor does it make [Icarom] an agency or instrumentality of the Republic of Ireland." *Id.*

1/ This doctrine is also referred to as collateral estoppel, but the term "issue preclusion" is preferred. *See, Robi v. Five Platters, Inc.*, 838 F.2d 318, 321 n.2 (9th Cir. 1988).

Because the Court finds the reasoning in both *Mobil* and *Murphy Oil* persuasive, the Court will exercise its discretion and apply the doctrine of issue preclusion to the question whether Icarom is an instrumentality of Ireland for FSIA purposes. *Davis & Cox v. Summa Corp.*, 751 F.2d 1507, 1519 (9th Cir. 1985) (decision to apply issue preclusion doctrine within the discretion of a district court). Here, the Court finds that despite receiving a full and fair opportunity to persuade the *Mobil* and *Murphy Oil* courts that it is a foreign instrumentality, those courts specifically concluded that it was not. In the Court's opinion, it is not an efficient use of judicial resources to repeatedly revisit the issue of Icarom's status under the FSIA. Finally, the Court notes that Icarom has presented no evidence which persuasively demonstrates that *Mobil* and *Murphy Oil* were wrongly decided.

For the foregoing reasons, the plaintiffs' motion to remand is GRANTED, and the court REMANDS this action to the King County Superior Court.

DATED this 9th day of April, 1993.

BRUCE RIFKIN, Clerk

By _____
Deputy Clerk

MURPHY OIL USA, INC., Plaintiff,

v.

UNITED STATES FIDELITY & GUARANTY COMPANY, Fidelity and Guaranty Insurance Underwriters, Inc., Lloyd's and Other Companies (Including Alba, Andrew Weir, Anglo-French Dominion, Drake, Edinburgh, English & American Economic, Excess, Fidelidade, Helvetia, London Overseas, Minster, Orion, River Thames, St. Helens, Sphere, Swiss Union, Threadneedle United Standard and World Auxiliary), Admiral Insurance Company, California Union Insurance Company, Employer's Surplus Lines Insurance Company, First State Insurance Company, Gibralter Casualty Company, Harbor Insurance Company, International Insurance Company, Stonewall Insurance Company, Twin City Fire Insurance Company, and Unigard Insurance Company, Defendants.

No. 91-1157.

United States District Court, W.D. Arkansas, El Dorado Division.

Dec. 21, 1992.

ORDER

HENDREN, District Judge.

Now on this 18th day of December, 1992, came to be heard the plaintiff's Motion to Remand. Three of the defendants have filed objections to the motion.

The Court has considered the pleadings and law relevant thereto, and finds as follows:

In its motion, plaintiff asserts five reasons for remand of this case:

1. The removal of the action from state court is a breach of contractual commitment of ICAROM p.l.c., successor in interest to the Insurance Corporation of Ireland (hereinafter collectively referred to as "ICI") to submit to any court of competent jurisdiction selected by Murphy, and Arkansas law of damages requires specific performance, and that ICI's contractual commitment to submit to Union county Circuit Court waived any arguable right ICI had to remove;

2. ICI has not met the burden of proof required to establish foreign state status under the FSIA, and in fact is not a foreign sovereign;

3. ICI was not an agency or instrumentality of a foreign state when policies 564/A20369 and 564/A22137 were sold to Murphy in 1967 and 1968, and therefore, ICI cannot assert foreign sovereign status in this matter;

4. ICI waited three (3) months to remove this matter, which is well past the thirty days required under 28 U.S.C. § 1446(b), and there is no evidence that such a delay was warranted;

5. Even if ICI could remove as a foreign sovereign, this court must remand the other parties since there is no independent basis for their removal.

On December 17, 1991, this action was removed from state court by ICAROM, p.l.c., successor in interest to the Insurance Corporation of Ireland ("ICI"). In the Notice of

Removal, ICI sets out the grounds for removal, including, *inter alia:*

> On December 4, 1991, plaintiff first identified Insurance Corporation of Ireland, predecessor in interest to ICAROM, p.l.c., as one of the company defendants named herein through production of policy information to counsel for Cheshire and Companies and, therefore, removal is timely under 28 U.S.C. Section 1441(d).
>
> * * *
>
> The above entitled and numbered cause is a suit of a civil nature at law and is one of which the district courts of the United States are given original jurisdiction in that it is a dispute between a resident of the United States and an agency or instrumentality of a foreign state, as defined in 28 U.S.C. Section 1603(b)(2), commonly referred to as the Foreign Sovereign Immunities Act (FSIA), all as more fully appears from the statements set forth in the Notice herein. Furthermore, this Court has pendent jurisdiction over plaintiff's state claims, if any.
>
> * * *
>
> ICAROM, p.l.c. is a corporation organized and existing pursuant to the laws of the Republic of Ireland. A majority of its shares or ownership interest is held and owned by the Republic of Ireland.

> ICAROM, p.l.c. is a "foreign state" within the meaning of 28 U.S.C. Section 1603(a) and does not claim immunity under 28 U.S.C. Sections 1605-1607 or any applicable international agreement in connection with the matters giving rise to the instant action. This Court, therefore, has original jurisdiction of this action pursuant to 28 U.S.C. Section 1330(a).

FORUM SELECTION CLAUSE

Plaintiff asserts that ICI, as well as other defendants in this action, contractually agreed to submit to suit in any court of competent jurisdiction chosen by Murphy, and in removing, has breached the terms of the contract. Plaintiff also asserts that this forum selection language constituted a waiver of the defendant's right to remove. Plaintiff states that under the policy, ICI agreed to the following provision, and defendants do not dispute said language appears in the policy:

> Service of Suit Clause
> It is agreed that in the event of the failure of Underwriters hereon to pay any amount claimed to be due hereunder, Underwriters hereon, at the request of the Assured, will submit to the jurisdiction of any Court of competent jurisdiction within the United States and will comply with all requirements necessary to give such Court jurisdiction and all matters arising hereunder shall be determined in accordance with the law and practice such Court. It is further agreed that service of process in such suit may be made as stated in Item 6 of the Declarations, and that in any suit instituted against any one of

> them upon this Policy, Underwriters will abide by the final decision of such court or of any Appellate Court in event of an appeal. The person or firm named in Item 6 are authorized and directed to accept service of process on behalf of underwriters in any such suit and/or upon the request of the assured to give a written undertaking to the assured that they will enter a general appearance upon Underwriters' behalf in the event such a suit shall be instituted.

In *Weltman v. Silna*, 879 F.2d 425 (8th Cir. 1989), *cert. denied,* --- U.S. ----, 112 S. Ct. 377 (1991), the plaintiff argued that the defendants waived their right to remove the suit to federal court when they consented to subject matter jurisdiction and venue in the state court in the City of St. Louis. The agreement in which the appellees consented to plaintiff's filing of the suit in state court did not address removal. The Court stated that waiver of the right to remove must be "clear and unequivocal," *id.* at 427, *citing* 1A J. Moore, B. Ringle & J. Wicker, Moore's Federal Practice ¶ 157.[9] (2d ed. 1987), and held that the district court properly rejected plaintiff's claims that the defendants waived their right to remove.

The requirement of "clear and unequivocal" language was also stated in *In re Delta America Re Ins. Co.*, 900 F.2d 890 (6th Cir. 1990), *cert. denied, Wright v. Arion Ins. Co.*, --- U.S. ----, 111 S. Ct. 233 (1990), which did involve the FSIA:

> . . . Although Congress made it very clear that foreign states have the right of removal, this does not mean, of course, that they may not waive that right. Against the backdrop of the FSIA, however, the principle that waiver must be clear and unequivocal

> assumes even greater significance. (footnotes omitted).

Id. at 893.

Other cases have held that a forum selection clause does not constitute a waiver. *Liberty Mut. Ins. v. Ins. Corp. of Ireland*, 693 F. Supp. 340, 347, n.2 (W.D. Pa. 1988) (an agreement to a forum consent clause does not constitute a waiver of the right to removal under FSIA, citing *Proyecfin de Venezuela, S.A. v. Banco Industrial de Venezuela S.A.*, 760 F.2d 390 (2d Cir. 1985) and Wright, Miller & Cooper, *Federal Practice and Procedure: Jurisdiction* 2d § 3729); *Regis Associates v. Rank Hotels (Management) Ltd.*, 894 F.2d 193 (6th Cir. 1990) (forum selection clause in hotel management contract, which did not explicitly refer to right of removal, did not constitute waiver of such right).

The following discussion is found in Wright, Miller & Cooper, *Federal Practice and Procedure: Jurisdiction 2d* § 3729 (1992 Supp.):

> One uncertainty under the new provision [28 U.S.C. Section 1441(d)] is whether a foreign state or an agency or instrumentality thereof may waive this right of removal. Since the Immunities Act provides for implicit or explicit waivers by the foreign state with regard to claims of sovereign immunity and for private agreements with regard to methods of service, but makes no parallel provision for waivers of the right of removal, it is likely that a federal court would accept removal jurisdiction of an action against a foreign state even in the face of an express waiver.

Other cases have held forum selection clauses do constitute a waiver. *Rose City v. Nutmeg Ins. Co.*, 931 F.2d 13 (5th Cir. 1991), *cert. denied,* --- U.S. ----, 112 S. Ct. 301 (1991) (held that the "service of suit" endorsement in a general liability policy, under which insurer agreed to submit to the jurisdiction of any court at the insured's request, foreclosed the insurer's right to remove state court action under the policy to federal court); *Mobil Corp. v. Abeille General Ins. Co.*, H-89-3877, 1990 U.S. Dist. LEXIS 19792 (S.D. Tex. 1990), *appeal pending,* No. 91-2401 (5th Cir.) (copy of which is attached to this Order) (holding that the burden is on the party seeking federal jurisdiction to "demonstrate that the case is within the competence of the Court," and that the defendants, one of whom is ICI, the same defendant now before this Court, failed to carry their burden of proving that they were "foreign sovereigns" or that the forum selection clause was ambiguous); *Capital Bank & Trust Co. v. Associated Int'l Ins. Co.*, 576 F. Supp. 1522 (M.D. La. 1984). The Court also notes that the Mobil Corp. court found that the policy involved therein was drafted by defendants and that it was ICI who inserted the service of suit provision.

The Court has reviewed the above cases carefully, and although the Court recognizes a close question is presented on this issue, the Court finds that the language contained in the agreement whereby ICI agrees to submit to "any Court of competent jurisdiction within the United States" is unambiguous and, constitutes a waiver of ICI's right to remove.

Furthermore, since this Court is holding that ICI has not established that it is a foreign state, as discussed below, those cases interpreting a forum selection clause as it relates to the FSIA, and any arguments that a foreign state's right to remove has priority over a forum selection clause are not applicable.

See Mobil Corp. v. Abeille General Ins. Co., H-89-3877, 1990 Dist. LEXIS 19792 (S.D. Tex. 1990), *appeal pending*, No. 91-2401 (5th Cir.).

WHETHER ICI HAS SUFFICIENTLY ESTABLISHED THAT IT IS A FOREIGN STATE FOR PURPOSES OF THE FSIA.

Even if the Court held otherwise on the forum selection clause issue, remand would nevertheless be appropriate since the Court is of the opinion that ICI has not sufficiently established that it is a foreign state for purposes of the FSIA. In the Notice of Removal, it is stated that ICAROM, p.l.c. is a "foreign state" for purposes of 28 U.S.C. § 1603(a).

> 28 U.S.C. § 1603(a) provides:
> For purposes of this chapter—
> (a) A "foreign state", except as used in section 1608 of this title, includes a political subdivision of a foreign state or an agency or instrumentality of a sovereign state as defined in subsection (b).
> (b) An "agency or instrumentality of a foreign state" means any entity—
> (1) which is a separate legal person, corporate or otherwise, and
> (2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof, and
> (3) which is neither a citizen of a State of the United States as defined in section 1332(c) and (d) of this title, nor created under the laws of any third county.

The entity claiming the protection of the statute has the burden of demonstrating, *inter alia:*

> that it falls within the statutory definition of a 'foreign state' or that it constitutes an entity 'a majority of whose shares or other ownership interest is owned by a foreign state.' 28 U.S.C. § 1603. Once a defendant presents prima facie evidence of this, the burden shifts to plaintiff to demonstrate that the Act does not apply. (citations omitted).

Outbound Maritime Corp. v. P.T. Indonesian Consortium, 575 F. Supp. 1222, 1224 (S.D.N.Y. 1983).

In addressing (b)(2) of § 1603, plaintiff argues that ICI has not met its burden of proof, relying heavily on the conclusions reached by the Court in *Mobil Corp.* Defendants submitted copies of district court cases which held otherwise, the one most directly on point being *In Re Texas Eastern Transmission Corp. Contamination Insurance Coverage Litigation,* MDL. 764 (E.D. Penn. Sept. 15, 1988). No Eighth Circuit case has been brought to the Court's attention resolving this issue. Therefore, the Court is left to decide, based upon the facts now before it, and the relevant case law, whether ICI is an agent or instrumentality of a foreign state for purposes of 28 U.S.C. § 1603.

The facts stated by the Texas district judge in *Mobil Corp.* are enlightening as they relate to this issue:

> Both ARIG and the ICI claim they are "foreign states" under the FSIA and as a result this Court has original jurisdiction under 28 U.S.C. Section 1330(a). There are three criteria to consider when deciding if a corporate entity is an agency or instrumentality of a foreign state. They are (1) the extent to which it performs a governmental function, (2) the degree to

which its operations are controlled by the state, and (3) whether it is organized under the laws of the sovereign in question. *Edlow International v. Nuklearna Electrarna Krsko,* 441 F. Supp. 827 (D.D.C. 1977). Since jurisdiction is determined at the time of removal, *see Morgan Guaranty Trust Co. of New York v. Republic of Palau,* 639 F. Supp. 706 (S.D.N.Y. 1986), this Court will not address the impending sale of ICI to a French insurance company.

* * * *

After Plaintiff filed its initial motion to remand a second "Notice of Removal and Joinder in Removal" was filed by Defendant ICI. ICI asserts that it too is a foreign sovereign under the FSIA making the removal proper. The evidence shows that on March 15, 1985 ICI was acquired by a new holding company, Sealuchais Arachais Teroanta ("SAT"). The Irish Minister for Industry, Trade, Commerce and Tourism allegedly assumed control of SAT and an administrator was appointed by the Irish High Court. It appears that this administrator is comparable to a trustee in bankruptcy or a rehabilitator in an insurance company rehabilitation because his primary function is to manage ICI as an ongoing concern in an attempt to place the company in a sound commercial and financial condition.

The evidence submitted to the Court contains a list of the shareholders of ICI as of April 2, 1990. Neither the Minister for Industry and Commerce nor the Irish government holds legal title to any stock in either ICI or SAT. Legal title to SAT's stock is in two individuals, Sean Martin Dorgan and Brid ni Uallachain as shown in the annual return of SAT filed July 6, 1987. It is these two individuals who have agreed to

hold their shares in trust for the benefit of the Minister of Industry and Commerce.

Even if the Irish government has an ownership interest in ICI this court's jurisdiction is not automatic. "Two more precise indices of an entity's status as a state agency or instrumentality focus on the degree to which the entity discharges a governmental function, and the extent of state control over the entities operations." *Edlow*, 441 F. Supp. at 832. No evidence has been submitted indicating ICI has a public purpose or that it is controlled by the government for any purpose except to see that its financial condition is restored.

To support its position ICI has submitted declarations of Andrew L. Banks, Chief Executive of ICI, and Liam MacGabhann, Assistant Principal Officer of the Department of the Irish Ministry of Industry and Commerce. Banks states in conclusory terms that ICI is wholly owned by the Republic of Ireland. However he concedes that "the purpose of the Administration was merely to ensure the continuation of the insurance business of ICI and the protection of all policy holders." He goes on to state that this situation is temporary and that as soon as ICI's financial condition is restored control of ICI will revert to its former shareholders and Board of Directors. Banks also admits that the only government connection is that shareholders of SAT hold their shares in trust for the Irish Minister of Finance.

On May 25, 1990 Mr. Banks was deposed. He states that Mr. McCann, ICI's administrator, is not a government employee and his fees are approved by the High Court and paid out of the assets of the company. Banks deposition p. 34. He also describes the powers of the Administrator and they appear to be almost identical to those of a liquidator. *Id.* p. 42-46. In addition, Mr. Banks did not suggest to the

Administrator that ICI attempt to invoke status as a foreign sovereign until 1987 or 1988. The company was placed in receivership in 1985. In the opinion of this Court the role of the Irish government in the affairs of ICIA does not constitute government ownership nor does it make ICI and [sic] agency or instrumentality of the Republic of Ireland.

Mr. MacGabhann is an official of the Ministry of Industry and Commerce and acts as a liaison between the Administrator and the Ministry. In his declaration he merely verifies that the declaration of Mr. Banks correctly states that the government owns ICI. No exhibits are attached. This is the only document submitted to the Court by a government official. Courts have refused to give credence to affidavits that are not supported by evidence of nationalization of a private enterprise or accompanied by documentation from the United States Department of State. *See Outbound Maritime Corporation v. P.T. Indonesian Consortium of Construction Industries,* 575 F. Supp. 1222 (S.D.N.Y. 1983).

* * *

After careful consideration the Court finds that ICI's assertion that it is a foreign sovereign is tenuous at best. "[T]]he burden of proof is upon the defendant to sustain federal jurisdiction [and] . . . where the court is in doubt, the motion to remand should be granted." *Jerro v. Home Lines, Inc.*, 377 F. Supp. 670, 672 (S.D.N.Y. 1984).

In the present case, Defendant submitted the Declaration of Brendan Murphy, General Manager of ICAROM prior to March 15, 1985, as well as the declaration of Mr. Laim MacGabhann, Assistant Principal Officer, Department of Industry & Commerce of the Government of Ireland in support of its position. In his Declaration, Murphy states, in pertinent part:

2. ICAROM was formerly known as the Insurance Corporation of Ireland plc ("ICI"). On August 1, 1990, ICI changed its name to ICAROM plc.

3. On March 15, 1985 ICAROM, then known as ICI, was acquired by the Government of Ireland when, by decision of the Government of Ireland, ownership of all shares of ICI was transferred from Allied Irish Banks plc to Sealuchais Arachais Teoranta ("SAT"), a new holding company.

4. Pursuant to specific statutory authority provided by the Insurance (Miscellaneous Provisions) Act, 1985 (copy attached as Exhibit A), the Government of Ireland, through the Minister for Industry, Trade, Commerce and Tourism (the "Minister") was authorized to take up shares in SAT and assume control of SAT.

5. More particularly, every member of SAT holds his shares in trust for the Minister such that the member is bound to pay every dividend or other money received in respect of such shares to the Minister and to transfer, as and when required by the Minister, such shares to the Minister or such other person nominated by the Minister. This relationship was given statutory recognition and established pursuant to Section 11 of the Insurance (Miscellaneous Provisions) Act, 1985.

6. Accordingly, SAT is nothing more than an organ though [sic] which by legislative fiat, the Government of Ireland is able to hold and control the shares of ICAROM.

7. On March 25, 1985, after the transfer of ownership had been effected, ICI was placed under administration pursuant to the provisions of the Insurance (No. 2) Act, 1983, by order of the High Court.

9. In sum, all shares in SAT are held in trust for the Minister, and all SAT Directors are Ministry employees. In turn, SAT holds all the shares of ICAROM. Consequently, the Government of Ireland, through SAT, has a clear and unequivocal ownership interest in ICAROM.

10. On July 31, 1990, ICAROM sold its business in the Republic of Ireland and Northern Ireland to Assurances Generales de France ("AGF"). The newly formed company acquiring this business trades under the name of the Insurance Corporation of Ireland plc.

11. ICAROM continues to run-off and administer the international business of the former Insurance Corporation of Ireland (with the exception of certain Marine Underwriting Agencies transferred with the Irish business). ICAROM is located in Dublin, Ireland, and still maintains a presence in London and other overseas locations.

12. Included in ICAROM's business controlled by the Government of Ireland are policies 564/A20369 and 564/A22137 issued to Murphy Oil.

In the Declaration of Liam MacGabhann, Mr. MacGabhann states that Murphy's declaration correctly states that "the ownership of Icarom plc. is in the Government of Ireland

through the Ministry for Industry & Commerce (formerly the Ministry for Industry, Trade, Commerce and Tourism.)"

It does not appear to the Court that the information submitted in this case varies greatly with that submitted in *Mobil Corp.*, and the Court finds the reasoning and conclusions reached by the court in *Mobil Corp.* to be persuasive. Furthermore, a persuasive reason in support of the position that ICI is not a foreign state is the principle that removal statutes will be strictly construed and doubt should be resolved in favor of state court jurisdiction. *Barnes v. Southwestern Bell Telephone Co.*, 596 F. Supp. 1046, 1048-49 (W.D. Ark. 1984) (citing *Shamrock Oil & Gas Corp. v. Sheets,* 313 U.S. 100 (1941)). In light of these general principles, after considering the facts in this case, the Court finds that the defendant ICAROM has failed to demonstrate to the Court that it is a foreign state.[1/]

Defendant states in the removal petition that this is a suit which the district courts of the United States are given original jurisdiction in that:

> it is a dispute between a resident of the United States and an agency or instrumentality of a foreign state, as defined in 28 U.S.C. Section 1603(b)(2), commonly referred to as the Foreign Sovereign Immunities Act (FSIA), all as more fully appears from the statements set forth in the notice herein. Furthermore, this Court has

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1/ The conclusion reached by the Court on this issue gives the defendant the benefit of the doubt on the issue concerning the time frame to be considered for purposes of removal. Defendants do not dispute that ICAROM was not a "FOREIGN STATE" during 1967 or 1968.

pendent jurisdiction over plaintiff's state claims, if any.

Since the Court has found that defendant ICI waived its right to remove, and that defendant ICI is not a foreign state under the FSIA, and since there appears to be no other basis for federal court jurisdiction, the Court is of the opinion that there is no need to address the remaining issues raised in the motion to remand, and the matter should therefore be remanded to the Circuit Court of Union County, Arkansas, Second Division. The Court will not exercise pendent jurisdiction over the remaining defendants.

IT IS SO ORDERED.

A-332

MOBIL CORPORATION, et al., Plaintiffs
v.
ABEILLE GENERAL INSURANCE CO., et al.,
Defendants.

Civ. A. No. H-89-3877.

United States District Court, S.D. Texas, Houston Division.

Nov. 6, 1990.

ORDER

NORMAN W. BEACH, Chief Judge.

Pending before the Court is Plaintiffs' motion to remand, Defendants' motions to dismiss, Defendants' motion to reconsider the order placing this case on the jury docket and ICI's motion to extend submission date. For the reasons set forth below the Court finds that the motion to remand should be granted making all other motions moot.

This suit was originally brought in state court seeking a declaratory judgment of Plaintiffs' rights under several insurance policies issued by Defendants. It was filed pursuant to the Texas Declaratory Judgment Act, Tex. Civ. Prac. & Rem. Code Ann. § 37.003 (Vernon 1986).

The case was removed in November 1989 by Defendant Arab Insurance Group ("ARIG") and numerous other Defendants. The basis for removal was (1) that Defendant ARIG is a foreign sovereign as that term is defined in the Foreign Sovereign Immunities Act, 28 U.S.C. § 1603 ("FSIA"); (2) there is federal jurisdiction; and (3) the amount in controversy exceeds $50,000 resulting in diversity jurisdiction. A motion to remand was timely filed

alleging this Court lacks subject matter jurisdiction and the case was improvidently removed. Thereafter a second "Notice of Removal and Joinder in Removal" was filed on behalf of the Insurance Corporation of Ireland ("ICI"). In that pleading ICI contends it too is a foreign sovereign for purposes of the FSIA.

Both ARIG and the ICI claim they are "foreign states" under the FSIA and as a result this Court has original jurisdiction under 28 U.S.C. § 1330(a). There are three criteria to consider when deciding if a corporate entity is an agency or instrumentality of a foreign state. They are (1) the extent to which it performs a governmental function, (2) the degree to which its operations are controlled by the state, and (3) whether it is organized under the laws of the sovereign in question. *Edlow International v. Nuklearna Electrarna Krsko,* 441 F. Supp. 827 (D.D.C. 1977). Since jurisdiction is determined at the time of removal, *see Morgan Guaranty Trust Co. of New York v. Republic of Palau,* 639 F. Supp 706 (S.D.N.Y. 1986), this Court will not address the impending sale of ICI to a French insurance company.

Defendant ARIG is owned jointly by the governments of Kuwait, Libya and the United Arab Emirates. According to a declaration by Bader A. Wahidi, an ARIG executive, the ARIG exists under the provisions of the Commercial Companies Law of Bahrain. When a corporation is organized under the laws of a third country which has no ownership interest in that corporation it cannot qualify as an agency or instrumentality of a foreign state. 28 U.S.C. § 1603(b)(3). Since ARIG is incorporated in Bahrain, which does not possess an ownership interest in ARIG, it cannot be a foreign sovereign under the FSIA and removal on this basis was improper. *See LeDonne v. Gulf Air, Inc.,* 700 F. Supp. 1400, 1406 (E.D. Va. 1988).

After Plaintiff filed its initial motion to remand a second "Notice of Removal and Joinder in Removal" was filed by Defendant ICI. ICI asserts that it too is a foreign sovereign under the FSIA making the removal proper. The evidence shows that on March 15, 1985 ICI was acquired by a new holding company, Sealuchais Arachais Teroanta ("SAT"). The Irish Minister for Industry, Trade, Commerce and Tourism allegedly assumed control of SAT and an administrator was appointed by the Irish High Court. It appears that this administrator is comparable to a trustee in bankruptcy or a rehabilitator in an insurance company rehabilitation because his primary function is to manage ICI as an ongoing concern in an attempt to place the company in a sound commercial and financial condition.

The evidence submitted to the Court contains a list of the shareholders of ICI as of April 2, 1990. Neither the Minister for Industry and Commerce nor the Irish government holds legal title to any stock in either ICI or SAT. Legal title to SAT's stock is in two individuals, Sean Martin Dorgan and Brid ni Uallachain as shown in the annual return of SAT filed July 6, 1987. It is these two individuals who have agreed to hold their shares in trust for the benefit of the Minister of Industry and Commerce.

Even if the Irish government has an ownership interest in ICI this court's jurisdiction is not automatic. "Two more precise indices of an entity's status as a state agency or instrumentality focus on the degree to which the entity discharges a governmental function, and the extent of state control over the entities operations." *Edlow*, 441 F. Supp. at 832. No evidence has been submitted indicating ICI has a public purpose or that it is controlled by the government for any purpose except to see that its financial condition is restored.

To support its position ICI has submitted declarations of Andrew L. Banks, Chief Executive of ICI, and Liam MacGabhann, Assistant Principal Officer of the Department of the Irish Ministry of Industry and Commerce. Banks states in conclusory terms that ICI is wholly owned by the Republic of Ireland. However he concedes that "the purpose of the Administration was merely to ensure the continuation of the insurance business of ICI and the protection of all policy holders." He goes on to state that this situation is temporary and that as soon as ICI's financial condition is restored control of ICI will revert to its former shareholders and Board of Directors. Banks also admits that the only government connection is that shareholders of SAT hold their shares in trust for the Irish Minister of Finance.

On May 25, 1990 Mr. Banks was deposed. He states that Mr. McCann, ICI's Administrator, is not a government employee and his fees are approved by the High Court and paid out of the assets of the company. Banks deposition p. 34. He also describes the powers of the Administrator and they appear to be almost identical to those of a liquidator. *Id.* p. 42-46. In addition, Mr. Banks did not suggest to the Administrator that ICI attempt to invoke status as a foreign sovereign until 1987 or 1988. The company was placed in receivership in 1985. In the opinion of this Court the role of the Irish government in the affairs of ICI does not constitute government ownership nor does it make ICI an agency or instrumentality of the Republic of Ireland.

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attached. This is the only document submitted to the Court by a government official. Courts have refused to give credence to affidavits that are not supported by evidence of nationalization of a private enterprise or accompanied by documentation from the United States Department of State. *See Outbound Maritime Corporation v. P.T. Indonesian Consortium of Construction Industries,* 575 F. Supp. 1222 (S.D.N.Y. 1983).

On April 10, 1990 this Court stayed all discovery until July 9 except on the issue of jurisdiction. This date was later extended to August 20. Plaintiffs noticed the depositions of Mr. Banks, Mr. MacGabhann and William McCann, an officer of the Irish High Court. However ICI will not produce Mr. MacGabhann or Mr. McCann because they are government employees and not within ICI's control. ICI is also unable to produce many requested documents which are possessed by either Mr. McCann or the Ministry of Commerce. The Court finds it hard to understand how ICI can be a government entity controlled by the Ministry of Commerce yet that governmental agency cannot now be compelled to participate in the discovery process.

After careful consideration the Court finds that ICI's assertion that it is a foreign sovereign is tenuous at best. "[T]he burden of proof is upon the defendant to sustain federal jurisdiction [and] . . . where the court is in doubt, the motion to remand should be granted." *Jerro v. Home Lines, Inc.,* 377 F. Supp. 670, 672 (S.D.N.Y. 1974).

Plaintiffs also allege that Defendants waived any right they may have had to removal by entering into insurance contracts containing a forum selection clause. The policies state "Underwriters hereon, at the request of the Assured, will submit to the jurisdiction of any Court of competent

jurisdiction within the United States and will comply with all requirements to give such Court jurisdiction and all matters arising hereunder shall be determined in accordance with the law and practice of such Court." Such language has been found to constitute a waiver. "The purpose of the service of suit clause is to allow a dissatisfied policy holder to compel the insurer to submit to the forum of the insured's choice to recover proceeds under the policy. By agreeing to 'submit' to a state forum, the defendant insurer waives the right to defend in federal court." *Capital Bank & Trust Co. v. Associated International Insurance Co.*, 576 F. Supp. 1522 (M.D. La. 1984) (citations omitted).

Defendants argue that there was no waiver because a foreign state's right to remove has priority over a forum selection clause. Since this Court has found none of the Defendants are foreign sovereigns this argument does not apply. In addition, in the case of ICI the evidence shows that shortly after his appointment the Administrator stated that his appointment would not bring about any change in the rights of policyholders under existing policies. Furthermore, the policy in question was drafted by Defendants and it is ICI who inserted the Service of Suit provision. It is well settled that when language in an insurance policy is susceptible to more than one interpretation it will be construed liberally in favor of the insured and strictly against the insurer; this is especially true when the dispute deals with exceptions and words of limitation. *Barnett v. Aetna Life Insurance Co.*, 723 S.W.2d 663 (Tex.1987). The policy in question, however, is unambiguous and clearly constitutes a waiver.

There is also no federal question jurisdiction in this matter. Plaintiff is seeking a declaration pursuant to a state declaratory judgment statute of its state law contract rights vis-a-vis the Defendants. To establish federal question

jurisdiction Plaintiffs must establish in their complaint a right to relief created by federal law. The complaint does not identify any law or statutes that would give rise to federal question jurisdiction. The existence of federal question jurisdiction is determined solely with reference to the well-pleaded allegations of the Plaintiffs' complaint. *See Oliver v. Trunkline Gas Co.*, 789 F.2d 341 (5th Cir. 1986).

Defendants contend that this Court must examine the allegations of the underlying causes of action which involve two federal statutes—the Employees Retirement Income Services Act ("ERISA") and the Age Discrimination in Employment Act ("ADEA"). The Court disagrees. This litigation involves the parties' rights and obligations under insurance contracts issued by Defendants to Plaintiffs and the duty to defend and indemnify. These are state law issues and do not raise a cause of action under any federal statute or common law. None of Plaintiffs' claims in this action are related in any way to either ERISA or the ADEA. No authority has been present by Defendants and the Court is unaware of any which demonstrate that federal question jurisdiction can be invoked in this situation. This claim simply does not arise under the laws of the United States.

In their response Defendants concede there is no diversity jurisdiction so that issue will not be addressed.

The Court has studied the numerous documents filed in this matter on the subject of removal and remand as well as the relevant caselaw. The burden is on the party seeking federal jurisdiction to "demonstrate that the case is within the competence of the Court." Wright, Miller & Cooper, Federal Practice and Procedure § 3522 (1984). Defendants

have not met their burden. For the reasons stated above, it is

ORDERED that Plaintiffs' motions to remand (entries 5, 32, and 58) are GRANTED and this case is REMANDED to the 11th Judicial District Court of Harris County, Texas. It is further

ORDERED that all other pending motions are MOOT.

IT IS SO ORDERED.

TEXAS EASTERN TRANSMISSION CORPORATION AFFILIATED COMPANIES*/

Panhandle Eastern Corporation
- Bison Insurance Company, Ltd.
  - Calidad Insurance, Ltd.
- Centana Energy Corporation
  - National Helium Corporation
- Centana Gathering Company
- Dixilyn-Field Drilling Company
  - Dixilyn-Field International Drilling Company, S.A.
  - Dixilyn-Field (Nigeria) Limited
- Energy Pipelines International Company
- Mantaray Pipeline Company
- Morgas, Inc.
- 1 Source Corporation
- Pan National Gas Sales, Inc.
- Pan Service Company
- Pan Transportation, Inc.
- Panhandle Acquisition Company
- Panhandle Eastern Pipe Line Company
  - Pan Border Gas Company
  - Pan Gas Storage Company
  - Panhandle Field Services Company
  - Panhandle Gathering Company
  - Trunkline Gas Company
- Panhandle Michigan Intrastate Company
- Panhandle Pipelines Operating Company
- Panhandle Storage Company

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*/ Excludes wholly-owned subsidiaries of Texas Eastern Transmission Corporation. Panhandle Eastern Corporation is the ultimate parent. Subsidiaries are indicated by indentation below their parents.

Panhandle Trading Company
Pantheon, Inc.
Pelmar Company
Source Cogeneration Company, Inc.
Texas Eastern Arkoma, Inc.
Panhandle Eastern Corporation (continued)
Texas Eastern Corporation
Algonquin Energy, Inc.
AGT Gateway Corp.
Algonquin Gas Transmission Company
Algonquin LNG, Inc.
Chambers County Land Company
Houston Center Corporation
Transwestern Gas Supply Company
Monument Intrastate Pipeline Company
Petroleum Services Holdings, Inc.
Eastman Whipstock do Brasil Ltda.
Eastman Whipstock, S.A.
Seahorse do Brasil Servicos Maritimos Ltda.
Summit Computing, Inc.
TEAL Lodge Company
Texas Eastern (Bermuda) Ltd.
Texas Eastern Arabian Ltd.
CTE Petrochemicals Company
Texas Eastern International Venturers, Ltd.
Texas Eastern Land Company, Inc.
Texas Eastern Products Pipeline Company
TE Products Pipeline Company, Limited Partnership
TEPPCO Partners, L.P.
Trans-Ohio Pipeline Company
Texas Eastern Oil Company
Texas Eastern Slurry Transport Company
Texas Eastern Transmission Corporation
Trunkline LNG Company

Supreme Court, U.S.
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No. 93-2070

In the Supreme Court of the United States

OCTOBER TERM, 1993

TEXAS EASTERN TRANSMISSION CORPORATION,
Petitioner,

v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,
Respondents.

On Petition For A Writ Of Certiorari ToThe United States Court of Appeals for the Third Circuit

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QUESTIONS PRESENTED

1. Whether the factual finding of the district court that the Insurance Corporation of Ireland was wholly owned by the Republic of Ireland and is therefore an "instrumentality of a foreign state" under 28 U.S.C. § 1603(b) was properly affirmed by the court of appeals as not clearly erroneous.

2. Whether, in an action based on diversity jurisdiction and governed by pre-1990 law now superseded by federal statute, there is ancillary jurisdiction over a defendant's compulsory counterclaim joining nondiverse parties pursuant to Fed. R. Civ. P. 13(h).

List of Affiliated Companies of Respondents
is found on pages RA6–RA43

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COUNTERSTATEMENT OF THE CASE

Petitioner Texas Eastern Transmission Corporation ("TETCO") is obligated, pursuant to consent decrees entered into with various federal and state agencies, to correct statutory violations and remediate environmental contamination at numerous sites along its interstate natural gas pipeline. Respondents are primary and excess insurers who issued policies of insurance under which Petitioner claimed insurance coverage for the cost of compliance with the consent decrees and related private party claims.

A. Three Separate Actions Consolidated

Petitioner's claims for insurance coverage were adjudicated in three actions which were ultimately consolidated in the United States District Court for the Eastern District of Pennsylvania as *"In re Texas Eastern Transmission Corp. PCB Contamination Insurance Coverage Litigation,"* MDL No. 764:

1. *F&C* action: In December 11, 1987, Fidelity & Casualty Co. of New York ("F&C") commenced a declaratory judgment action against Petitioner in the Northern District of Texas, with jurisdiction based on diversity of citizenship. The *F&C* action was transferred by the Judicial Panel for Multidistrict Litigation to the Eastern District of Pennsylvania in May 1988 as part of MDL No. 764.

2. *AEGIS* action: On March 11, 1988, Associated Electric & Gas Insurance Services Limited ("AEGIS") and another excess insurer commenced a declaratory judgment action in the Eastern District of Pennsylvania against Petitioner and all of its other insurers, including

the Insurance Corporation of Ireland ("ICI").[1] Jurisdiction in the *AEGIS* action was predicated, *inter alia*, upon the Foreign Sovereign Immunities Act ("FSIA"), in that ICI was, at the time of suit, wholly owned by the Republic of Ireland, and so was an "instrumentality of a foreign state" within the meaning of 28 U.S.C. § 1603(a) and (b).

3. *Texas Eastern* action: On March 21, 1988, Petitioner filed a declaratory judgment and breach of contract action in Texas state court against all of its insurers, including ICI.[2] ICI removed the case to the United States District Court for the Southern District of Texas pursuant to 28 U.S.C. § 1441(d). The court transferred the case to the Eastern District of Pennsylvania under 28 U.S.C. § 1404(a), where it was consolidated with the other two actions in MDL No. 764.

B. Respondents Prevail on the Merits

In July 1992, the district court granted summary judgment to all Respondents denying Petitioner's claims for insurance coverage. *See* A-106 to A-281. Judgment in favor of all Respondents was entered individually in each of the three cases which comprise

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[1]In addition to Petitioner's insurers, the Pennsylvania Insurance Guaranty Association is also a Respondent in the *AEGIS* action.

[2]Petitioner initially filed suit against all of its insurers in New Jersey state court and moved to stay or dismiss the *F&C* action in Texas in favor of its New Jersey action. Petitioner filed the *Texas Eastern* action only after its New Jersey suit was dismissed on grounds of *forum non conveniens* on March 17, 1988.

MDL No. 764. A-278 to A-281. The court of appeals affirmed the grant of summary judgment in favor of Respondents on the merits in all three cases. A-36, A-51 to A-64.

Petitioner does not seek certiorari on the merits of its claim for insurance coverage. Rather, it raises two jurisdictional questions, one relating to the *AEGIS* and *Texas Eastern* actions, and another arising in the *F&C* action. The Court is respectfully referred to the opinions below for a more detailed discussion of the merits. The following facts pertain to the jurisdictional issues raised in the Petition before the Court.

C. The District Court Upholds Jurisdiction in All Three Actions

In July 1988, Petitioner moved for remand of the *Texas Eastern* action to Texas state court and dismissal of the *AEGIS* action for lack of jurisdiction under the FSIA. In support of FSIA jurisdiction, Respondent ICI submitted the affidavit of its chief executive officer, which set forth facts showing that ICI met each of the three statutory elements to constitute an instrumentality of a foreign state under § 1603(b). A-296. With respect to the majority ownership element in § 1603(b)(2), the affidavit stated that "in March 1985 the Government of Ireland acquired 100 percent shares of ICI through a wholly owned corporation." *Id.* Petitioner raised numerous arguments against FSIA jurisdiction which it has since abandoned. With respect to ICI's status, Petitioner argued that ICI was merely under administration "similar to a Chapter 11 proceeding under United States Bankruptcy laws" and was not actually owned by the Irish government. A-297. Petitioner did not contend, as it does now, that

ICI's status should be determined on criteria other than ownership.

The district court rejected Petitioner's argument, stating that "although ICI may be under the administration of the Courts for some purposes, a majority of the shares of ICI, 'or other ownership interests' is owned by the Republic of Ireland." A-298. The district court explained:

> [Section 1603(b)(2)] provides that it be a majority of the shares or other ownership interest. Since SAT owns 100 percent of ICI's shares and SAT is 100 percent owned and controlled by the Republic of Ireland through its Minister of Industry and Commerce, and the sole shareholders and directors of SAT are officials of the Department of Industry and Commerce, *there is a direct and complete ownership of ICI by the Republic of Ireland for purposes of 28 USC Section 1603.*

A-298 (emphasis added). In support of its finding of "direct and complete ownership," the district court cited the Irish enabling statute for SAT, which provided, among other things, that the Irish Minister was granted "all of the rights and powers" of a shareholder, and that any dividends and profits "were to go to the Exchequer of Ireland." A-297. Accordingly, the district court denied Petitioner's challenges to FSIA jurisdiction in the *Texas Eastern* and *AEGIS* actions.

At this time, F&C and Petitioner were still the only parties in the *F&C* action. Diversity jurisdiction was unchallenged in the *F&C* action, but Petitioner had asked for reconsideration of its motion to stay or

dismiss, which had been denied twice already in the Northern District of Texas prior to transfer to MDL No. 764. The district court denied reconsideration and made clear that all three cases would be consolidated and proceed with coordinated discovery and preparations for trial. A-290 to A-291; A-307 to A-308.

After its jurisdictional objections were denied, Petitioner answered the F&C complaint. As a "precautionary measure," it joined the excess insurers as additional parties to its compulsory counterclaim against F&C pursuant to Fed.R.Civ.P. 13(h). A-14 to A-17; Petition at 8. Petitioner alleged that there was "ancillary jurisdiction" over the excess insurers, A-17, and that all its insurers were *"jointly and severally"* liable for all of Petitioner's claims. A-19 n.5 (emphasis by the court). F&C and most of the excess insurers have citizenship diverse from Petitioner; six of the excess insurers are nondiverse. Petition at 8. Thus, "[w]hat started out as an action between only [F&C] and [Petitioner] then became, through [Petitioner's] actions, a case involving *all* [Respondents]." A-13 (emphasis by the court). As noted above, the district court ultimately granted summary judgment in favor of all Respondents in all three actions.

D. The Court of Appeals Upholds Jurisdiction in All Three Actions.

On appeal,[3] Petitioner initially challenged jurisdiction only in the *AEGIS* and *Texas Eastern*

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[3]While appealing the judgment of the district court, Petitioner also commenced an action in Texas state court as an attempted collateral attack. The new action was removed to federal court and transferred to the Eastern District of Pennsylvania, where it was consolidated with a

actions, on grounds not raised in the Petition. Petitioner did not assign error to the factual finding that ICI was an instrumentality of a foreign state because it was owned by the Republic of Ireland. Rather, in a footnote, Petitioner suggested that the "ownership" test was inappropriate and argued only that ICI could not be considered an "instrumentality" of Ireland because ICI was controlled by an administrator who did not exercise functions that are "peculiarly governmental." Brief for Appellant TETCO at 68 n.89 (No. 92-1638).

In its initial May 28, 1993 opinion, the Court of Appeals upheld FSIA jurisdiction in the *AEGIS* and *Texas Eastern* actions based on "the presence as a defendant of ICI, which qualifies as a foreign state because the Republic of Ireland owns 100% of its stock and has assumed its obligations." A-81; see also A-94 n.1. The court then affirmed the district court's exercise of FSIA jurisdiction, rejecting Petitioner's claims of error as to waiver and realignment. A-81 to A-83. The court (and the dissent) found diversity jurisdiction in the *F&C* case. A-81; A-93.

On June 10, 1993, Petitioner filed a petition seeking both panel rehearing and rehearing in banc solely on the basis that the court's rulings as to realignment in the *AEGIS* case and waiver of the right to remove in the *Texas Eastern* case were in conflict with Third Circuit precedents. Petitioner did not seek rehearing with

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similar action filed in response by one Respondent. The district court, by order dated April 21, 1994, stayed proceedings and barred the commencement of any further PCB-related insurance coverage litigation pending resolution of this Petition, even if Petitioner is the target of new claims by third-parties. A-2 to A-3.

respect to the status of ICI as an instrumentality of a foreign state or the district court's jurisdiction over the excess insurers in the *F&C* action. Petitioner then—for the first time—took the position that the excess insurers were not in fact parties to the *F&C* action because Petitioner had failed to cause summonses to be served on them. A-17. The panel granted rehearing "limited exclusively to the matters raised in the petition," and requested further briefs addressing three specific jurisdictional issues. A-74.

Upon rehearing and reargument, the Court of Appeals found that all Respondents were parties to the *F&C* action, A-14 to A-17, and again affirmed federal jurisdiction in all three actions. A-36. The January 10, 1994 opinion confirms that Petitioner did not challenge the finding that ICI was a "foreign state" but, rather, assumed that ICI was an instrumentality of a foreign state and challenged jurisdiction on other grounds. A-14. Nevertheless, confirming its own jurisdiction, the Court of Appeals affirmed the finding that ICI was a "foreign state" as "not clearly erroneous." A-23 n.8. The dissent did not disagree, assuming that ICI "falls within 28 U.S.C. § 1603's definition of a 'foreign state'" and dissenting on other grounds. A-39.

With respect to the *F&C* action, the Court of Appeals held that it is "undisputed" that the court had diversity jurisdiction over the initial claims of F&C against Petitioner. A-14. The dissent concurred. A-46. The Court of Appeals then turned to Petitioner's challenge to ancillary jurisdiction "over the nondiverse counterclaim defendants" based on *Finley v. United States*, 490 U.S. 545 (1989). A-17. The court noted that, prior to *Finley*, the Third Circuit had held that ancillary jurisdiction could be exercised over additional parties

to a compulsory counterclaim. *Id.* The court found that *Finley* involved pendent jurisdiction over a claim by a plaintiff in a suit under the Federal Tort Claims Act, while the present case involved ancillary jurisdiction over parties added by a defendant to a compulsory counterclaim. A-17 to A-19. The court noted that "'the bringing in of additional parties to respond to a compulsory counterclaim does not destroy diversity jurisdiction,'" A-20 to A-21, and that there would be supplemental jurisdiction in such circumstances under 28 U.S.C. § 1367, although that statute did not apply by its terms. A-21. Accordingly, the court concluded that *Finley* was not controlling and that "the additional non-diverse counterclaim defendants do not destroy diversity jurisdiction in the *F&C* action." A-21.

On January 24, 1994, Petitioner filed a second rehearing petition seeking only rehearing in banc. The second rehearing petition assumed for purposes of argument that ICI was an instrumentality of a foreign state. The Third Circuit denied rehearing on February 3, 1994. A-4 to A-5.

REASONS FOR DENYING THE PETITION

The Court of Appeals has affirmed judgment on the merits in favor of Respondents in three consolidated cases and upheld federal jurisdiction in each on alternative grounds. Petitioner's first question would affect jurisdiction in the *AEGIS* and *Texas Eastern* actions. Petitioner's second question addresses jurisdiction only in the *F&C* action, and only with respect to some Respondents in that action. Even if this Court were to grant review and Petitioner were to prevail on both questions, there would still be federal

jurisdiction over most Respondents in the third action, and the judgment rendered in their favor would be unaffected. Dismissal with prejudice and collateral estoppel would then be proper for the remaining Respondents.

Neither of the questions presented calls for this Court's review. The first involves only a factual determination of the legal status of a single corporation. There is no conflict among the courts of appeals and no indication that the circumstances of the corporation are of any general importance. The second question has no prospective importance. In 1990, Congress enacted a statute, 28 U.S.C. § 1367, which controls all cases filed on or after December 1, 1990. As to the few cases still governed by pre-1990 law, such as this one, there is no conflict among the courts of appeals on the narrow question presented of ancillary jurisdiction over compulsory counterclaims against nondiverse parties added by defendants under Fed. R. Civ. P. 13(h). Moreover, as noted above, the answer to the second question will have little if any practical significance even for the parties.

I. Certiorari Is Not Warranted to Review the Factual Finding of Both Courts Below That ICI Is an Instrumentality of a Foreign State.

A. This Case Presents No Legal Issue of General Importance

The courts below asserted federal jurisdiction over the *AEGIS* and *Texas Eastern* actions on the basis of a factual determination that ICI is an "instrumentality of a foreign state." 28 U.S.C. § 1603(b). The statute

defines an "agency or instrumentality of a foreign state" to be *"any entity"*

> (1) which is a separate legal person, corporate or otherwise, and
>
> (2) ... a majority of whose shares *or other ownership interest* is owned by a foreign state or political subdivision thereof, and
>
> (3) which is neither a citizen of a State of the United States as defined in [28 U.S.C. § 1332(c)-(d)], nor created under the laws of any third country.

28 U.S.C. § 1603(b) (emphasis added).

There has never been any dispute concerning the first and third of these criteria. At the district court, Petitioner argued that the second criteria was not satisfied because ICI was merely under court-supervised administration similar to United States bankruptcy proceedings. A-297. The district court rejected the analogy, holding that "there is a direct and complete ownership of ICI by the Republic of Ireland for purposes of 28 USC Section 1603." A-298. That determination was supported by a number of specific findings:

- "SAT owns 100 percent of ICI's shares and SAT is 100 percent owned and controlled by the Republic of Ireland through its Minister of Industry and Commerce." A-298.
- The Irish Minister of Industry and Commerce is specifically empowered by an

Irish statute to "exercise all of the rights and powers of holders of shares" and "the sole shareholders and directors of SAT have been two officials of the Department of Industry and Commerce." A-297.

- All dividends and profits of ICI go, through SAT, to the Exchequer of Ireland. A-297.

- Since March 1985, ICI had been "operated by an Administrator appointed by the [Irish] Government." A-296.

- The Administrator "is entitled to the powers of management and shareholder." A-297.

These findings plainly distinguish the Irish government's ownership of ICI from United States bankruptcy proceedings. Dividends and profits of a company in reorganization are not paid into the United States treasury.

The Court of Appeals affirmed the district court's factual finding of majority ownership by the Irish government, applying the "clearly erroneous" standard of review.[4] A-23 n.8. (The dissent simply assumed that ICI was an instrumentality of a foreign state and

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[4]It is well-settled that district courts may make necessary factual findings for purposes of determining federal subject matter jurisdiction and that those factual findings are reviewed under the "clearly erroneous" standard. *See, e.g., Land v. Dollar*, 330 U.S. 731, 735 n.4 (1947); *Herbert v. National Academy of Sciences*, 974 F.2d 192, 197-98 (D.C. Cir. 1992); *Williamson v. Tucker*, 645 F.2d 404, 413 (5th Cir.), *cert. denied*, 454 U.S. 897 (1981).

dissented on other grounds, which are not raised in the Petition. A-39 to A-42.)

The lower court's factual findings present no legal questions calling for this Court's review. *Rudolph v. United States*, 370 U.S. 269, 270 (1962); *Rogers v. Lodge*, 458 U.S. 613, 623 (1982). Petitioner's belated attempt to inject a legal issue into the determination of ICI's status as an instrumentality of a foreign state is unavailing; that determination is so fact-specific to ICI that even the "mixed" question is inappropriate for review.

Petitioner's fact-bound question does not present an issue of importance to anyone other than the parties. Petitioner attempts to fabricate an issue of more general significance by erroneously implying that the decision below would make any insolvent foreign company an instrumentality of a foreign state and thereby unleash an avalanche of litigation in the federal courts. Petition at 15. Petitioner errs, first, in characterizing ICI as insolvent. In fact, the Irish government's assumption of ownership of ICI *prevented* insolvency. Petitioner errs, secondly, in confusing government administration of an insolvent enterprise with government ownership of an enterprise. The facts in this case establish "direct and complete ownership" by a foreign state. A-298. The numerous indicia of ownership found by the district court in this case were critical in establishing the majority ownership interest required by § 1603(b)(2). These indicia of ownership will not be present in typical insolvency proceedings. Court-appointed administrators may have management powers over an insolvent enterprise, but the government does not thereby assume actual ownership and collect the dividends and profits from the enterprise.

Thus, Petitioner's suggestion that the decision below presages massive abuse of the FSIA by insolvent foreign insurance companies is baseless. The predicted avalanche of litigation has simply not occurred, almost six years after the district court's ruling. Petitioner has been unable to point to a single insolvent foreign insurer during that period that has claimed FSIA jurisdiction based on governmental ownership. In fact, such a prospect is unlikely because insolvency typically results in a stay of legal proceedings, and so an insolvent will generally have no occasion to invoke FSIA jurisdiction. *Cf.* 11 U.S.C. § 362 (automatic stay of proceedings against debtor under bankruptcy law).

B. There is No Conflict Among the Circuits

The courts of appeals have repeatedly and consistently upheld jurisdiction under the FSIA when "a majority of [a corporation's] shares *or other ownership interest* is owned by a foreign state." 28 U.S.C. § 1603(b)(2) (emphasis added).[5] The broad "other

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[5]Recent decisions include, *e.g., Commercial Bank of Kuwait v. Rafidain Bank*, 15 F.3d 238, 239 (2d Cir. 1994) ("a commercial bank wholly owned by the Republic of Iraq" is "therefore" an agency or instrumentality of a foreign state); *NYSA-ILA Pension Trust Fund v. Garuda Indonesia*, 7 F.3d 35, 37, 38 (2d Cir. 1993) (FSIA jurisdiction over a "corporation that is owned entirely by a foreign state"), *cert. denied*, 114 S.Ct. 1065 (1994). The statutory standard of majority ownership is so straightforward that it is commonly undisputed. *See, e.g., Sugimoto v. Exportadora de Sal, S.A. de C.V.*, 19 F.3d 1309, 1310 (9th Cir. 1994) ("a manufacturer of salt owned 51 percent by the government of Mexico and 49 percent by Mitsubishi Corporation"); *Drexel Burnham Lambert Group Inc. v. Committee of Receivers*, 12 F.3d 317, 320, 324 (2d Cir. 1993) (a committee formed by the Emirate of Dubai to "wind up the business

ownership interest" provision in the statute makes clear that the foreign state is allowed flexibility in selecting a legal or corporate structure for holding its majority ownership interest.

Petitioner argues that the Irish government cannot exercise its rights under the FSIA because it "has at most an indirect interest in ICI's shares." Petition at 12. Nothing in the statute or in the precedents of this Court or the courts of appeals suggests that the form of ownership employed was insufficient in any respect. The district court relied on the "other ownership interest" provision in rejecting that argument. A-298. Other courts have similarly upheld FSIA jurisdiction without regard to the technical form of ownership.[6]

Petitioner concedes that there is no *actual* conflict among the circuits and argues only that there is a "functional equivalent" of a conflict based on "three district court decisions holding that ICI is not a foreign state." Petition at 13. The Court's settled practice is to

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affairs and liquidate all nonbanking assets" was "an instrumentality of the Emirate"), *cert. denied*, 114 S.Ct. 1644 (1994); *Rodriguez v. Transnave, Inc.*, 8 F.3d 284, 286 & n.1 (5th Cir. 1993) (a ship "wholly owned by... a state naval entity of Ecuador").

[6]*See, Cargill Int'l. S.A. v. M/T Pavel Dybenko*, 991 F.2d 1012, 1015-16 (2d Cir. 1993); *Chuidian v. Philippine Nat. Bank*, 912 F.2d 1095, 1098 (9th Cir. 1990); *O'Connell Mach. Co. v. M.V. "Americana,"* 734 F.2d 115, 116-17 (2d Cir.), *cert. denied*, 469 U.S. 1086 (1984); *Talbot v. Saipem A.G.*, 835 F. Supp. 352, 353 n.2 (S.D. Tex. 1993); *Balentine v. Union Mortgage Co.*, 795 F. Supp. 266, 267-69 (N.D. Ill. 1992); *Trump Taj Mahal Assoc. v. Costruzioni Aeronautiche Giovanni Augusta, S.p.A.*, 761 F.Supp. 1143, 1149-50 (D.N.J. 1991), *aff'd*, 958 F.2d 365 (3d Cir.), *cert. denied*, 113 S.Ct. 84 (1992).

leave the resolution of conflicts among district courts to the courts of appeals. Petitioner asserts that the Court should abandon that practice because Congress's bar on appellate review of certain remand orders, *see* 28 U.S. § 1447(d), prevents conflicts among the circuits from arising.

Petitioner has overlooked the fact that actions against an instrumentality of a foreign state are within the original jurisdiction of the federal courts under 28 U.S.C. § 1330(a) (as in the *AEGIS* action) and 28 U.S.C. § 1332(a)(4) (foreign state plaintiff) as well as the removal jurisdiction under 28 U.S.C. § 1441(d) (as in the *Texas Eastern* action). Section 1447(d) does not limit appellate review of determinations of original jurisdiction. The courts of appeals have applied and interpreted § 1603(b)(2) in the many cases that are not within the scope of Congress's bar on appellate review. *See, e.g.*, p.13 n.5; p.14 n.6. These decisions of the courts of appeals are not in conflict, and there is no reason for the Court to begin undertaking to reconcile district court decisions, particularly unpublished district court decisions.

The fact that all three district court opinions on which Petitioner relies are unpublished—with limited precedential value even in the district courts—greatly weakens Petitioner's claim that they deserve to be considered the "functional equivalent" of decisions of the courts of appeals. Consideration of their specific holdings and circumstances confirms that these particular opinions are not such "functional equivalents."

One of the district court opinions on which Petitioner relies was undercut by the Eighth Circuit on

appeal. *Murphy Oil USA, Inc. v. United States Fidelity & Guar. Co.*, No. 93-1207 (8th Cir. June 21, 1993) (RA-1 to RA-3). Petitioner reprinted the district court's opinion in *Murphy Oil, see* Petition at 13-14, A-316 to A-331, but did not inform the Court of the decision on appeal. The Eighth Circuit found the factual record before it insufficient and remanded the case to the district court for "a more detailed presentation and analysis of the facts" bearing upon the question of whether ICAROM (a successor of ICI) was an instrumentality of a foreign state.[7] RA-2. The court of appeals recognized that the determination of whether ICI is a "foreign state" is fact-bound and implicitly rejected the district court findings on which Petitioner relies. The Eighth Circuit's order in *Murphy Oil* certainly does not conflict with the decisions below and renders untenable Petitioner's claim that the district court opinion in *Murphy Oil* should be considered the functional equivalent of a decision by the Eighth Circuit.[8]

The remaining district court opinion cited by Petitioner as establishing a conflict among the circuit courts is *Mobil Corp. v. Abeille Gen. Ins. Co.*, No H-89-3877, 1990 WL 504828 (S.D. Tex. Nov. 6, 1990), *appeal dismissed*, 984 F.2d 664 (5th Cir. 1993). A-332 to A-339. The court in *Mobil* applied a non-statutory "public

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[7]The court of appeals retained jurisdiction to proceed with the appeal following the evidentiary hearing in the district court. RA-2 to RA-3. The appeal was subsequently dismissed pursuant to Fed. R. App. P. 42(b). *Murphy Oil* (8th Cir. Aug. 30, 1993); RA-5.

[8]*Aluminum Co. of America v. Admiral Ins. Co.*, No. C93-32C (W.D. Wash. Apr. 9, 1993), also cited by Petitioner, held only that ICAROM lacked standing to remove, while, in dicta, indicating it would follow *Murphy* and *Mobil*. A-313 to A-315.

purpose" test to determine whether ICI was an instrumentality of a foreign state and stated that "[n]o evidence has been submitted indicating ICI has a public purpose." A-334. Applying its non-statutory test, and based on the particular record before it and its dissatisfaction with discovery responses, the district court concluded that "ICI's assertion that it is a foreign sovereign is tenuous at best." A-336.

The *Mobil* court derived its non-statutory jurisdictional test (which Petitioner seizes upon here), from another district court opinion in *Edlow International Co. v. Nuklearna Elektrarna Krsko*, 441 F.Supp. 827 (D.D.C. 1977). Petition at 14. In *Edlow*, a workers' organization operating a power plant in Yugoslavia argued that it was an "organ" or an "instrumentality" of a foreign state because "all property under a socialist system ... is subject to the ultimate ownership and authority of the state." *Id.* at 831. The *Edlow* court's discussion of the degree of governmental function and control—on which the district court in *Mobil* based its "public purpose" test—simply explains *Edlow*'s conclusion that entities in a socialist state are not all automatically "organs" of the state on that basis. *Cf. S&S Mach. Co. v. Masinexportimport*, 706 F.2d 411, 415 & n.3 (2d Cir.) (trading company wholly owned by Romanian government was an "instrumentality" of a foreign state; *Edlow* distinguished), *cert. denied*, 464 U.S. 850 (1983).

Relying on the district court opinions in *Mobil* and *Edlow*, Petitioner argues that review is appropriate to consider whether two vague and subjective requirements should be added to the three set forth in the FSIA definition of an "instrumentality of a foreign state." In Petitioner's view, the statute should be read

to require consideration of "the *degree* to which the entity discharges a government function," and "the *extent* of state control over the entity's operations." Petition at 14 (emphasis added). Petitioner relegated this argument to a brief footnote in the court of appeals, *see* pp.5-6, *supra*, and the courts below did not address it.

Petitioner's argument is unsupportable under any theory of statutory interpretation, and there is no conflict among the courts of appeals warranting this Court's review. In any event, Petitioner's two proposed new jurisdictional requirements would plainly be satisfied on the record before the Court, so resolution of the issue would make no difference in the result in this case. The *Mobil* court did not offer any rationale for its adoption of *Edlow*'s comments on applying the FSIA to entities in socialist states, which, in effect, would write those comments into § 1603(b) as new jurisdictional requirements. The plain language of the statute forecloses any such result. None of the three criteria in § 1603(b) suggests that FSIA jurisdiction turns on the discharge of a government function or control of day-to-day operations.

The adoption of the vague *Edlow* criteria, as suggested by Petitioner, would undercut Congress's efforts to set forth clear-cut standards for jurisdictional rulings under the FSIA so that foreign states would respect decisions of the federal courts and grant fair treatment to United States interests abroad in return. Foreign states might understandably perceive decisions based on Petitioner's vague criteria as subject to political manipulation and less worthy of respect, contrary to Congress's purpose. In addition, the legislative history of the FSIA evidences Congress's

expectation that commercial enterprises owned by foreign states would be classed as instrumentalities under the statute.[9]

Petitioner did not press the issue of its two proposed new jurisdictional requirements below or make a record sufficient to preserve it for review. Even if it had, jurisdiction would be unaffected, because both proposed requirements are satisfied on the record before the Court. As to the degree of state control, ICI is "100 percent owned *and controlled*" by the Irish government. A-298 (emphasis added). As to discharge of a government function, the Irish statutes cited by the district court are conclusive. These statutes specifically authorize the Irish government's ownership and control of ICI. A-297 to A-298. In *First National City Bank v. Banco Para el Comercio Exterior de Cuba*, 462 U.S. 611, 624-27 (1983), this Court identified enabling statutes such as those cited by the district court as a "typical" characteristic of an "instrumentality" under the FSIA and explained the important governmental functions performed by such instrumentalities.

Accordingly, review should be denied because the factual determination of ICI's status as an instrumentality of a foreign state presents no legal issue of any importance and there is no conflict among the courts of appeals.

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[9] *See* H. R. Rep. No. 94-1487, 94th Cong., 2d Sess. (1976), *reprinted in* 1976 U.S.C.C.A.N. 6614 (examples of commercial instrumentalities include "a state trading corporation, a mining enterprise, a transport organization such as a shipping line or airline, a steel company, a central bank, an export association").

II. Certiorari Is Not Warranted to Review a Narrow Question of Ancillary Jurisdiction Over the Nondiverse Excess Insurers in the *F&C* Action.

A. Petitioner's Second Question Has No Prospective Importance and Is Moot for Most Respondents.

Petitioner seeks review of a narrow question of ancillary jurisdiction pertaining only to the *F&C* action—whether a defendant may add nondiverse parties to a compulsory counterclaim pursuant to Fed. R. Civ. P. 13(h). Although inapplicable to this case, 28 U.S.C. § 1367 answers that question as to all cases commenced on or after December 1, 1990. A-21 n.7 (supplemental jurisdiction would exist under § 1367); Petition at 21 n. 12. Consequently, that question has no prospective importance whether or not Petitioner is correct in its reading of *Finley v. United States*, 490 U.S. 545 (1989); and we believe it is not. Any decision by this Court would affect very few other cases.

In addition, Petitioner's question only addresses jurisdiction over its "counterclaims against nondiverse parties."[10] Question 2, Petition at i. Since the final judgment entered against Petitioner in favor of its primary insurer and the diverse excess insurers in the *F&C* action would not be affected, Petitioner's question

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[10] *See* Petition at 18 (*Finley* prohibits pendent-party jurisdiction over "added parties over whom no independent basis of jurisdiction exists"); Petition at 9, 10, 17, 18, 21 (challenging jurisdiction over "nondiverse excess insurers").

not only lacks any general importance, it has no significance even as to most Respondents.[11]

B. There Is No Conflict Among the Circuits

Petitioner has framed its question presented in terms of "pendent-party jurisdiction" under *Finley v. United States*, 490 U.S. 545 (1989) (applying Federal Tort Claims Act). Petitioner asserted ancillary jurisdiction in the district court, however, not pendent-party jurisdiction. A-17. On appeal, the Court of Appeals held that there was ancillary jurisdiction, and distinguished pendent-party jurisdiction. A-17 to A-21. The Court of Appeals carefully considered *Finley's* holding that pendent-party jurisdiction does not allow a plaintiff to join non-governmental parties under the Federal Tort Claims Act, and correctly concluded that there was no conflict between *Finley* and its decision upholding ancillary jurisdiction over nondiverse parties joined by a defendant to a compulsory counterclaim under Rule 13(h).[12] A-17 to A-21.

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[11]The Court of Appeals unanimously rejected Petitioner's contention that the entire judgment should be vacated so that the action could be remanded to state court, explaining that "it would be extremely imprudent to remand this cause on the basis of what amounts to conjecture on the part of [Petitioner], which cannot call into question the competence of a federal court to resolve matters of substantive state law." A-15.

[12]The Court recently emphasized that in considering ancillary jurisdiction, "[i]t is to the holdings of our cases, rather than their dicta, that we must attend." *Kokkonen v. Guardian Life Ins. Co.*, 114 S.Ct. 1673, 1676 (1994). That caution seems particularly apt with respect to *Finley*, since the Court acknowledged the pragmatic benefits of pendent party jurisdiction and invited Congress to act.

Pendent-party jurisdiction typically involves claims by a *plaintiff* against a party the plaintiff could not have directly named as a defendant because of restrictions on federal jurisdiction. Thus, the Court in *Finley* declined to permit the *plaintiff* to assert claims against nondiverse parties where the basis for federal jurisdiction, the FTCA, only authorized suits against the United States. Similarly, in *Owen Equipment & Erection Co. v. Kroger*, 437 U.S. 365, 374-75 (1978), the Court did not allow the *plaintiff* to assert claims against a nondiverse third-party defendant, emphasizing that otherwise the fundamental requirement of complete diversity might be "evaded completely."[13] In contrast, ancillary jurisdiction "typically involves 'claims by a

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Finley, 490 U.S. at 555-56. Congress responded by promptly enacting the supplemental jurisdiction statute. As the Fifth Circuit concluded, "'[I]t would make no sense to give an expansive reading to *Finley* to reach a result that Congress has deliberately repudiated for future cases.' C.A. Wright, et al., Federal Practice and Procedure § 3567.2 (Supp. 1992)." *Rodriguez v. Pacificare of Texas, Inc.*, 980 F.2d 1014, 1019 (5th Cir.), *cert. denied*, 113 S.Ct. 2456 (1993). *See Ponce Fed. Bank, F.S.B. v. Vessel Lady Abby*, 980 F.2d 56, 59 (1st Cir. 1992) (same, *quoting* Professor Wright).

[13]Petitioner has never disputed that the requirement of complete diversity is satisfied in the *F&C* action between the original parties: plaintiff F&C and defendant Petitioner. The Court of Appeals noted that "the bringing in of additional parties to respond to a compulsory counterclaim does not destroy diversity jurisdiction." A-20 to A-21, *quoting* C.A. Wright, LAW ON FEDERAL COURTS § 79 at 527 n.6 (4th ed. 1983). Even if there were a problem, it could be easily cured by the dismissal with prejudice of the nondiverse parties. *See Newman-Green, Inc. v. Alfonzo-Lorrain*, 490 U.S. 826, 836 (1989) ("requiring dismissal [of the entire case] after years of litigation would impose unnecessary and wasteful burdens on the parties, judges, and other litigants waiting for judicial attention").

defending party haled into court against his will, or by another person whose rights might be irretrievably lost unless he could assert them in an ongoing action in federal court.'" A-19, *quoting Owen*, 437 U.S. at 376.

Petitioner is the *defendant* in the *F&C* action, not the plaintiff and, thus, was "haled into court against [its] will." *Id.* Petitioner asserted a compulsory counterclaim against plaintiff F&C (its primary insurer) and joined its excess insurers as additional defendants to this counterclaim pursuant to Rule 13(h). It concedes that it asserted ancillary jurisdiction as a "precautionary measure" to protect its rights. Petition at 8. This is the same type of situation the Court identified in *Owen* as justifying ancillary jurisdiction for claims by a defendant but not by a plaintiff. Thus, the Court of Appeals correctly found that upholding ancillary jurisdiction over the nondiverse excess insurers was consistent—not in conflict—with *Finley* and *Owen*.[14]

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[14]The Court of Appeals noted that this distinction between claims by plaintiffs (which might undermine the complete diversity rule) and claims by defendants (which do not pose the same danger) is preserved by the supplemental jurisdiction statute. A-20 to A-21. Petitioner ignores the fact that 28 U.S.C. § 1367(b) only restricts supplemental jurisdiction over "claims by *plaintiffs*" in diversity cases. A-20 (emphasis by the court), *quoting* § 1367(b). Prof. McLaughlin, on whom Petitioner mistakenly relies, Petition at 21 n.12, indicates only that supplemental jurisdiction should not extend to claims *by a plaintiff* against parties joined under Rule 13(h), *e.g.*, claims by plaintiff F&C against nondiverse excess insurers. McLaughlin, *The Federal Supplemental Jurisdiction Statute—A Constitutional and Statutory Analysis*, 24 Ariz. St. L.J. 849,940 (1992). This case involves a claim *by a defendant* joining nondiverse parties under Rule 13(h). Prof. McLaughlin agrees with Respondents that there is

The Third Circuit decision is consistent not only with *Finley* but also with decisions of other courts of appeals. It was generally accepted prior to the enactment of the supplemental jurisdiction statute that ancillary jurisdiction extended to nondiverse parties added by a defendant pursuant to Rule 13(h) in a compulsory counterclaim. *See, e.g., Zurn Indus. v. Action Constr. Co.*, 847 F.2d 234, 238 (5th Cir. 1988); *Bauer v. Uniroyal Tire Co.*, 630 F.2d 1287, 1290 n.2 (8th Cir. 1980); *Newburger, Loeb & Co. v. Gross*, 563 F.2d 1057, 1070 (2d Cir. 1977), *cert. denied*, 434 U.S. 1035 (1978); *United Artists Corp. v. Masterpiece Prod., Inc.*, 221 F.2d 213, 217 (2d Cir. 1955) (Clark, J.); *see also Owen Equip.*, 437 U.S. at 375 n.18; C.A. Wright, LAW ON FEDERAL COURTS § 9 at 31 (4th ed. 1983) ("Ancillary jurisdiction permits courts to ... bring in additional parties to respond to a compulsory counterclaim under Rule 13(h)"). This rule continued unchanged subsequent to *Finley:*

> Prior to the *Finley* decision, it was well-settled that when diversity between parties is lacking, a court could assert ancillary jurisdiction over an additional party joined to a compulsory counterclaim pursuant to rule 13(h). [citations omitted]. We believe that *Finley* does not invalidate this widely accepted practice.

Associated Dry Goods Corp. v. Tower Fin. Corp., 920 F.2d 1121, 1125 (2d. Cir. 1990).[15]

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jurisdiction over such claims under the law before *Finley*, under the law after *Finley*, and under the supplemental jurisdiction act. *Id.* at 876, 927, 931-32, 937, 947.

[15]Ancillary jurisdiction over the nondiverse excess insurers would also be available by treating Petitioner's

The Court recently stated that "[g]enerally speaking, we have asserted ancillary jurisdiction (in the very broad sense in which that term is sometimes used) ... to permit disposition by a single court of claims that are, in varying respects and degrees, factually interdependent." *Kokkonen v. Guardian Life Ins. Co.*, 114 S.Ct. 1673, 1676 (1994). The assertion of ancillary jurisdiction in the *F&C* action is clearly appropriate as it involves a compulsory counterclaim (*i.e.*, a claim arising out of the same transaction or occurrence) in which Petitioner sought a finding of joint and several liability against all its insurers on virtually identical claims arising from a common nucleus of operative facts. A-19 n.5.

Birmingham Fire Ins. Co. of Pa. v. Winegardner & Hammons, Inc., 714 F.2d 548 (5th Cir. 1983), the only circuit court case cited by Petitioner as conflicting with the decision below, is plainly distinguishable on this ground. *Birmingham Fire* involved a claim which was "most definitely not a compulsory counterclaim." *Id.* at

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Rule 13(h) counterclaims against the nondiverse excess insurers as Rule 14(a) third-party claims. *See, e.g., Schwab v. Erie Lackawanna R.R. Co.*, 438 F.2d 62, 64 (3d Cir. 1971) (treating compulsory counterclaim as third-party claim and upholding ancillary jurisdiction). Ancillary jurisdiction over third-party claims against nondiverse parties was "well-settled" prior to *Finley*. *Id.* at 65; 6 C. Wright & A. Miller, FEDERAL PRACTICE & PROCEDURE § 1444 (2d ed. 1990) ("it is well settled that there need be no independent jurisdictional basis for [defendant's claims against a third-party defendant] if diversity of citizenship exists between the original parties"). This rule also remained settled after *Finley*. *See, e.g., King Fisher Marine Serv., Inc. v. 21st Phoenix Corp.*, 893 F.2d 1155, 1158, 1161 (10th Cir.), *cert. denied*, 496 U.S. 912 (1990); *Washington Hosp. Ctr. v. Collier*, 947 F.2d 1498, 1500-01 (D.C. Cir. 1991).

552. There were no allegations of joint and several liability, and the claims were sufficiently unrelated that the court questioned whether there was even a "common nucleus of operative fact," the constitutional minimum requisite for ancillary jurisdiction. *Id.*, *quoting United Mine Workers v. Gibbs*, 383 U.S. 715, 725 (1966). *Cf. Zurn Indus.*, 847 F.2d at 236-38 (Fifth Circuit decision upholding ancillary jurisdiction over nondiverse parties added by Rule 13(h) to a compulsory counterclaim); *Syndicate 420 at Lloyd's London v. Glacier Gen. Ins. Co.*, 633 F.Supp. 428, 431-32 (E.D. La. 1986) (distinguishing *Birmingham Fire* as involving claims which "were not interrelated").

Accordingly, review should be denied because there is no conflict among the courts of appeals, and the question presented has no prospective significance and is moot as to most Respondents.

CONCLUSION

The petition for a writ of certiorari should be denied.

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Decision of the U.S. Court of Appeals for the Eighth Circuit Dated June 21, 1993 (Pages RA1-RA3)

United States Court of Appeals

FOR THE EIGHTH CIRCUIT

No. 93-1207

Murphy Oil USA, Inc.,

Appellee,

v.

United States Fidelity and Guaranty Company; Fidelity and Guaranty Insurance Underwriters, Inc.,

Defendants

Lloyd's of London, also known as Scottish Lion Insurance Company, Inc., also known as Insurance Corporation of Ireland, also known as World Auxiliary, also known as United Standard, also known as Threadneedle, also known as Swiss Union, also known as Sphere, also known as St. Helens, also known as River Thames, also known as Orion, also known as Minster, also known as London Overseas, also known as Helvetia, also known as Fidelidad, also known as Excess, also known as English & American, also known as Edinburgh, also known as Drake, also known as Anglo-French, also known as Andrew Weir, also known as Alba, also known as Insurance Company

of North America, also known as Dominion Insurance Company Ltd.,

Appellant.

Admiral Insurance Company; California Union Insurance Company; Employer's Surplus Lines Insurance Company; First State Insurance Company; Gilbraltar Casualty Company; Harbor Insurance Company; International Insurance Company; Stonewall Insurance Company; Twin City Fire Insurance Company; Unigard Insurance Company; Associated International Company,

Defendants.

No. 91-1157

Appeal from the United States District Court for the Western District of Arkansas.

Before BOWMAN, Circuit Judge, HEANY, Senior Circuit Judge, and BEAM, Circuit Judge.

An issue in this matter is whether Insurance Company of Ireland (ICI) now known as ICAROM plc (ICAROM) is an agency or instrumentality of a foreign state, as defined by 28 U.S.C. § 1603(b)(2). The district court found that "based upon the facts now before it" ICAROM failed to demonstrate that it was a "foreign state." We believe that this finding requires a more detailed presentation and analysis of the facts bearing upon the subject.

We retain jurisdiction of this appeal and remand the case to the district court for a hearing on this issue. The

district court shall conduct an evidentiary hearing on whether ICAROM is or is not an agency or instrumentality of a foreign state and shall, within 90 days, certify its findings of fact and conclusions of law to this court.

Upon the filing of the district court's certification, the clerk shall notify the parties. They shall then have 20 days after notification to file simultaneous briefs limited to this issue. Thereafter, the matter shall stand submitted to this panel for decision.

June 21, 1993

Order Entered at the Direction of the Court:
s/
Clerk, U.S. Court of Appeals, Eighth Circuit

Judgment of the U.S. Court of Appeals for the Eighth Circuit Dated August 30, 1993 (Pages RA4-RA5)

United States Court of Appeals

FOR THE EIGHTH CIRCUIT

No. 93-1207

Murphy Oil USA, Inc.,

Appellee,

v.

United States Fidelity and Guaranty Company; Fidelity and Guaranty Insurance Underwriters, Inc.,

Defendants

Lloyd's of London, also known as Scottish Lion Insurance Company, Inc., also known as Insurance Corporation of Ireland, also known as World Auxiliary, also known as United Standard, also known as Threadneedle, also known as Swiss Union, also known as Sphere, also known as St. Helens, also known as River Thames, also known as Orion, also known as Minster, also known as London Overseas, also known as Helvetia, also known as Fidelidad, also known as Excess, also known as English & American, also known as Edinburgh, also known as Drake, also known as Anglo-French, also known as Andrew Weir, also known as Alba, also known as Insurance Company

of North America, also known as Dominion Insurance Company Ltd.,

Appellant.

Admiral Insurance Company; California Union Insurance Company; Employer's Surplus Lines Insurance Company; First State Insurance Company; Gilbraltar Casualty Company; Harbor Insurance Company; International Insurance Company; Stonewall Insurance Company; Twin City Fire Insurance Company; Unigard Insurance Company; Associated International Company,

Defendants.

No. 91-1157

Appeal from the United States District Court for the Western District of Arkansas.

JUDGMENT

Appellant's motion to dismiss the appeal is granted. The appeal is hereby dismissed in accordance with Federal Rules of Appellate Procedure 42(b).

The Court's mandate shall issue forthwith.

August 30, 1993

A true copy.

Attest: s/
Clerk, U.S. Court of Appeals,
Eighth Circuit

LIST OF AFFILIATED COMPANIES OF RESPONDENTS[1]
(Pages RA6-RA43)

Fidelity & Casualty Ins. Co. of New York

Parent: The Continental Corporation

Associated Electric & Gas Insurance Services Limited

None

Aetna Casualty and Surety Company

Parent: Aetna Life and Casualty Company

American Home Assurance Company

Subsidiary of: American International Group, Inc.

Boston Old Colony Insurance Company

Parent: The Continental Corporation

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[1]Respondents make this disclosure as required by Supreme Court Rule 29.1. Although CIGNA Insurance Company and the Insurance Company of North America are identified as "respondents" by TETCO, TETCO has not challenged the grant of summary judgment in their favor on other grounds.

Continental Casualty Company

Parent: CNA Financial Corporation
Loew's Corporation

Employers Mutual Company

First State Insurance Company

Parent: ITT Corporation

Subsidiaries: New England Insurance Corporation and New England Reinsurance Company

Highlands Insurance Company

Subsidiary of: Halliburton Company

The Home Insurance Company

Parent: Home Holdings, Inc.

Insurance Company of the State of Pennsylvania

Subsidiary of: American International Group, Inc.

International Insurance Company

International Insurance Company is a subsidiary of the Resolution Group, Inc., which is a subsidiary of Talegen Holdings, Inc. The parent of Talegen Holdings, Inc. is Xerox Financial Services, Inc. The parent of Xerox Financial Services, Inc. is Xerox Corp.

Lexington Insurance Company

Parent: American International Group, Inc.

Subsidiary of:
Birmingham Fire Insurance Company, Insurance Company of the State of Pennsylvania, and National Union Fire Insurance Company of Pittsburgh, PA.

National Surety Corporation

National Surety Corporation is a subsidiary of Fireman's Fund Insurance Company, which is a subsidiary of Allianz of America, which is a subsidiary of Allianz Aktiengesellschaft Holding of Germany.

Pennsylvania Insurance Guaranty Association

None

Prudential Reinsurance Company

Subsidiary of:
The Prudential Insurance Company of America

Ranger Insurance Company

Subsidiary of: Fairfax Financial Holdings

Republic Insurance Company

Republic-Vanguard Insurance Company is a wholly-owned subsidiary of Republic Insurance Company, a subsidiary of Republic-Vanguard Reinsurance Co. Republic-Vanguard Reinsurance Co. is a subsidiary of Republic Financial Services, Inc. of Nevada, which is a subsidiary of Republic Financial Services, Inc. of Texas. Republic Financial Services, Inc. of Texas is a subsidiary of Winterthur U.S. Holdings, Inc., a subsidiary of Winterthur Swiss Insurance Co. of Switzerland. The only publicly owned company is Winterthur Swiss Ins. Co. of Switzerland.

Stonewall Insurance Company

Subsidiary of: Great American Insurance Company

United States Fire Insurance Company

United States Fire Insurance Company is a subsidiary of Crum & Forster Holdings, Inc. Crum & Forster Holdings, Inc. is a subsidiary of Talegen Holdings, Inc. The parent of Talegen Holdings, Inc. is Xerox Financial Services, Inc. The parent of Xerox Financial Services, Inc. is Xerox Corp.

Certain Underwriters at Lloyd's, London

Parent Companies: None

Subsidiaries (except for wholly-owned): None

London Market Insurance Companies

Agrippina Versicherungs Aktiengesellshaft Insurance Company, Limited

Parent Companies:
The majority of Agrippina Versicherungs Aktiengesellshaft Insurance Company, Limited's shares are owned by Zurich Insurance Company, Switzerland.

Subsidiaries (except for wholly owned):
Agrippina Lebensversicherung Aktiengesellschaft; Agrippina Ruckversicherung Aktiengesellschaft and Patria Versicherung Aktiengesellschaft.

Allianz International Insurance Company, Limited

Parent Companies:
Allianz International Insurance Company, Limited is now known as Allianz Cornhill International plc. The company is owned by Allianz (UK) Ltd. (37.5%) and Cornhill Insurance plc (62.5%). The ultimate parent company is Allianz Aktiengesellschaft (AG) Holding.

Subsidiaries (except for wholly-owed): None.

Anglo Saxon Insurance Association, Limited

Parent Companies:
Anglo Saxon Insurance Association, Limited, now known as Unione Italiana (U.K.) Reinsurance Company Limited, is wholly-owned by Unione Italiana di Riassicurazione SpA.

Subsidiaries (except for wholly-owned): None.

Assicurazioni Generali SpA Insurance Company (United Kingdom), Limited

Parent Companies:
Assicurazioni Generali SpA Insurance Company (United Kingdom), Limited is a wholly-owned subsidiary of Assicurazioni Generali SpA.

Subsidiaries (except for wholly-owned): None.

Assurances Generales de France (UK) IART

Parent Companies:

Assurances Generales de France (UK) IART is wholly-owned by Assurances Generales de France IART, which in turn is owned by Assurances Generales de France, S.A. (86.2%) and Société Centrale Des Assurances Generale de France.

Subsidiaries (except for wholly-owned): None.

Atlantic Mutual Insurance Company, Limited

Parent Companies:

Atlantic Mutual Insurance Company, Limited is wholly-owned by the Atlantic Mutual Insurance Company.

Subsidiaries (except for wholly-owned): None.

Atlas Assurance Company, Limited

Parent Companies:

Atlas Assurance Company, Limited is wholly-owned by GRE (U.K.) Ltd. The ultimate holding company is Guardian Royal Exchange plc.

Subsidiaries (except for wholly-owned): None.

Baloise Fire Insurance Company, Limited

Parent Companies:
Baloise Fire Insurance Company, Limited is a wholly-owned subsidiary of Baloise Holding, the parent company of the Baloise Group.

Subsidiaries (except for wholly-owned): None.

Baltica-Skandinavia, Insurance Company (United Kingdom) Limited

Parent Companies:
Baltica-Skandinavia, Insurance Company (United Kingdom) Limited, now known as Baltica Insurance Company (UK) Limited, is a wholly-owned subsidiary of Baltica Forsikring A/S.

Subsidiaries (except for wholly-owned): None.

Bellefonte Insurance Company, Limited

Parent Companies:
Bellefonte Insurance Company, Limited was merged into the Northwestern National Insurance Group, whose immediate parent is Armco Financial Services Corp., and whose ultimate parent is Armco Inc.

Subsidiaries (except for wholly-owned): None.

Bishopsgate Insurance Company, Limited

Parent Companies:

The immediate parent of Bishopsgate Insurance Company, Limited is Fortis, Inc. The ultimate parent companies are the N.V. AMEV and Groupe AG.

Subsidiaries (except for wholly-owned): None.

British Aviation Insurance Company, Limited

Parent Companies:

British Aviation Insurance Company, Limited's stock is owned by the following companies: Sun Alliance and London Insurance plc. (29.74%); Commercial Union Assurance Co. plc (29.68%); Royal Insurance plc (27.37%); General Accident & Life Assurance Corporation plc (8.46%) and Guardian Assurance Co. Ltd. (4.75%).

Subsidiaries (except for wholly-owned): None.

British Law Insurance Company, Limited

Parent Companies:

British Law Insurance Company, Limited is a wholly-owned subsidiary of Sun Alliance and London Insurance plc., which in turn is wholly-owned by Sun Alliance Group plc.

British Merchants' Insurance Company, Limited

Parent Companies:
British Merchants' Insurance Company, Limited merged into Dominion Insurance Company Limited. Its immediate holding company is Dominion Insurance Limited and its ultimate holding company is Fondiaria, SpA.

Subsidiaries (except for wholly-owned): None.

British National Life Insurance Society, Limited

Parent Companies:
British National Life Insurance Society, Limited is now known as British National Life Assurance Company Limited. Its immediate holding company is CI Services Holdings Limited, and its ultimate holding company is Wingfield Limited.

Subsidiaries (except for wholly-owned): None.

British Northwesten Insurance Company, Limited

Parent Companies:
The parent company of British Northwestern Insurance Company, Limited is Eagle Star Insurance Company Limited, which in turn, is wholly-owned by Eagle Star Holdings plc., which in turn is a wholly-owned subsidiary of BAT Industries plc.

Subsidiaries (except for wholly-owned): None.

British Reserve Insurance Company, Limited

Parent Companies:

The immediate parent of British Reserve Insurance Company, Limited is Cornhill Insurance plc. The ultimate parent is Allianz Versicherungs-AG, which, in turn, is a wholly-owned subsidiary of Allianz AG Holding.

Subsidiaries (except for wholly-owned): None.

C.F. & A.U., Limited

Parent Companies:

The immediate holding company of C.F. & A.U., Limited is B.D. Cooke & Partners and its ultimate holding company is Fondiaria, SpA.

CNA Reinsurance of London, Limited

Parent Companies:

CNA Reinsurance of London, Limited, now known as CNA International Reinsurance Co. Ltd., is a wholly-owned subsidiary of Continental Casualty Company, which is controlled by CNA Financial Corporation. The ultimate parent company is Loews Corporation.

Subsidiaries (except for wholly-owned): None.

Colbourne Insurance Company, Limited

Parent Company:
The parent of Colbourne Insurance Company, Limited is Coastal Corporation.

Subsidiaries (except for wholly-owned): None.

Commercial Union Assurance Company of the United Kingdom, Limited

Parent Companies:
Commercial Union Assurance Company plc is the parent of Commercial Union Assurance Company of the United Kingdom, Limited. Commercial Union plc is the ultimate parent company.

Subsidiaries (except for wholly-owned): None.

La Concorde

Parent Companies:
La Concorde's three major shareholders are Generali France (62.4%), Assurances Generales de Trieste et Venise (10%) and Assicurazioni Generali SpA (9.4%). The company is ultimately controlled by the Generali Group, Italy.

Subsidiaries (except for wholly-owned):
Compagnie Continentale d'Assurances; La Federation Continentale; Europeene de Protection Juridique; La Lutece; La Reunion

Francaise and L'Equite and Northern Star Insurance Company.

Continental Insurance Company, Limited

Parent Companies:

The Continental Insurance Company, Limited is now known as the Continental Insurance Company (Europe) Limited. The immediate parent company is Lombard Continental Insurance plc. The company's ultimate parent is The Continental Corporation.

Subsidiaries (except for wholly-owned): None.

Cornhill Insurance plc

Parent Companies:

Allianz (U.K.) Limited is the immediate parent of Cornhill Insurance plc. Allianz Versicherungs-AG is its ultimate parent. Allianz Versichrungs-AG is a wholly-owned subsidiary of Allianz AG Holding.

Subsidiaries (except for wholly-owned): None.

Dai Tokyo Insurance Company, Limitied

Parent Company:

Dai Tokyo Insurance Company, Limitied is a wholly-owned subsidiary of The Dai Tokyo Fire & Marine Insurance Company, Limited.

Subsidiaries (except for wholly-owned): None.

Devonport Insurance Company, Limited

Parent Companies:

Devonport Insurance Company, Limited is now known as Sovereign Insurance (U.K.) Ltd., which is a wholly-owned subsidiary of Sovereign Marine & General Insurance Company Limited which, in turn, is wholly-owned by Willis Corroon plc.

Dominion Insurance Company

Parent Companies:

The immediate holding company of Dominion Insurance Company Limited is Dominion Insurance Holdings Limited and its ultimate holding company is Fondiaria, SpA.

Subsidiaries (except for wholly-owned): None.

Drake Insurance Company, Limited

Parent Companies:

Drake Insurance Company Limited was merged into Sphere Drake Insurance plc. Its immediate holding company is Sphere Drake Insurance Group plc which is, in turn, wholly-owned by Sphere Drake Acquisitions Limited which is, in turn, wholly-owned by Sphere Drake Holding plc (U.K.), which is, in turn, wholly-owned by SD Holding Limited which is, in turn, wholly-

owned by Sphere Drake Holdings Limited (Bermuda).

Subsidiaries (except for wholly-owned): None.

Edinburgh Assurance Company, Limited

Parent Companies:
The parent company of Edinburgh Assurance Company, Limited is Commercial Union plc.

Elders Insurance Company, Limited

Parent Companies:
Elders Insurance Company, Limited is a subsidiary of Sun Alliance and London plc.

English and Scottish Insurance Company, Limited

Parent Companies:
English and Scottish Insurance Company, Limited is a subsidiary of AXA Marine & Aviation Insurance (U.K.) Limited. The ultimate parent company is AXA S.A. (France).

Ennia (United Kingdom)

Parent Companies:
Ennia is a wholly-owned subsidiary of AEGON General Insurance Holdings (U.K.) Limited. The ultimate parent company is AEGON NV.

Subsidiaries (except for wholly-owned): None.

L'Etoile S.A.

Parent Companies:
L'Etoile S.A. is wholly-owned by AG 1824 (Compagnie Belge d'Assurances Generales). The shares of AG 1824 are held by N.V. AMEV (50%) and Groupe AG (50%).

Subsidiaries (except for wholly-owned): None.

Excess Insurance Company, Limited

Parent Companies:
Excess Insurance Company, Limited is a wholly-owned subsidiary of London & Edinburgh Insurance Group, Limited which in turn is wholly-owned by Hartford International Insurance Company which in turn is owned by ITT Corporation.

Subsidiaries (except for wholly-owned): None.

Fugi Fire and Marine Insurance Company (United Kingdom), Limited

Parent Companies:
Fugi Fire and Marine Insurance Company (United Kingdom), Limited, now known as Fugi International Insurance Company Ltd., is a subsidiary of The Fugi Fire & Marine Insurance Company Limited. The parent company's

shares trade on the Tokyo and Osaka Stock Exchange.

Subsidiaries (except for wholly-owned): None.

Group Josi per Thilly Re, Belgium

Parent Companies:
Sofina S.A. is the immediate parent of Group Josi. The ultimate parent is Assuranz Group Josi.

Subsidiaries (except for wholly-owned): None.

GTE Insurance Company, Limited

Parent Companies:
GTE Insurance Company, Limited, now known as Greyfriars Insurance Company Limited, is a wholly-owned subsidiary of Sovereign Marine & General Insurance Company Limited which is wholly-owned by Willis Corroon plc.

Guarantee Insurance Company

Parent Companies:
The Guarantee Insurance Company is wholly-owned by the Thomson Corporation (Canada).

Hansa Marine Insurance Company, Limited

Parent Companies:
The immediate holding company of Hansa Marine Insurance Company, Limited is Trygg-Hansa Forsakring AB. The ultimate holding company is Trygg-Hansa SPP Holding AB.

Highlands Insurance Company, Limited

Parent Companies:
The immediate parent of Highlands Insurance Company, Limited is Halliburton Holdings Ltd. The ultimate parent is Halliburton Company.

Subsidiaries (except for wholly-owned): None.

Indemnity Marine Insurance Company, Limited

Parent Companies:
Indemnity Marine Insurance Company, now known as Indemnity Marine Assurance Company, is a wholly-owned subsidiary of Commercial Union Assurance Company, plc. The ultimate parent company is Commercial Union, plc.

Subsidiaries (except for wholly-owned): None.

INSCO

Parent Companies:
INSCO is a wholly-owned subsidiary of Bermaco Insurance Co. Ltd. Bermaco Insurance

Co. Ltd. is a member of the Chevron Corporation Group of Companies.

Subsidiaries (except for wholly-owned): None.

Insurance Company of North America (United Kingdom), Limited

Parent Companies:
Insurance Company of North America (United Kingdom), Limited is a wholly-owned subsidiary of CIGNA U.K. Holdings Limited. The ultimate holding company is CIGNA Corporation.

Subsidiaries (except for wholly-owned): None.

Insurance Corporation of Ireland, Limited

Parent Companies:
Insurance Corporation of Ireland, Limited, now known as Icarom plc, is wholly-owned by ministers of, and in trust for, the government of the Republic of Ireland.

Subsidiaries (except for wholly-owned):
Property Corporation of Ireland, Ltd.

Lincoln Insurance Company, Limited

Parent Companies:
The Lincoln Insurance Company, Limited is wholly-owned by the Thomson Corporation (Canada).

Subsidiaries (except for wholly-owned): None.

Lloyd Italico Assicurazioni

Parent Companies:
The immediate parent of Lloyd Italico Assicurazioni is Royal Insurance plc. Royal Insurance Holdings plc. is the ultimate parent of Lloyd Italico Assicurazioni.

Subsidiaries (except for wholly-owned): None.

London & Edinburgh General Insurance Company, Limited

Parent Companies:
London & Edinburgh General Insurance Company, Limited (also known as London & Edinburgh Insurance Company, Limited) is a wholly-owned subsidiary of London & Edinburgh Insurance Group Limited which is, in turn, owned by Hartford International Insurance Company which is, in turn, owned by ITT Corporation.

Subsidiaries (except for wholly-owned):
Excess Underwriting Management Singapore Limited.

London & Hull Maritime Insurance Company, Limited

Parent Companies:
London & Hull Maritime Insurance Company, Limited is now known as AXA Marine & Aviation Insurance Co. Ltd., and is part of the AXA Group. AXA S.A. (France) is the ultimate parent company.

Subsidiaries (except for wholly-owned): None.

London & Overseas Insurance Company, Limited

Parent Companies:
London & Overseas Insurance Company, Limited is a wholly-owned subsidiary of Orion Insurance Company plc., which in turn, is a wholly-owned subsidiary of Nationale-Nederlanden (U.K.) Ltd., which in turn is a wholly-owned subsidiary of Internationale Nederlanden Verzekeringen NV (parent).

Subsidiaries (except for wholly-owned): None.

Minster Insurance Company, Limited
Parent Companies:
Minster Insurance Company, Limited is now known as GAN Minster Insurance Company Ltd. The company is a wholly-owned subsidiary

of GAN International S.A. The ultimate holding company is Société Centrale du Groupe Assurances Nationales.

Subsidiaries (except for wholly-owned):
The Contingency Insurance Company, Ltd.

National Security Fire and Casualty Company

Parent Companies:
The parent company of National Security Fire and Casualty Company is National Security Group, Inc.

Subsidiaries (except for wholly-owned): None.

Nippon Fire and Marine Insurance Company (U.K.) Limited

Parent Companies:
Nippon Fire and Marine Insurance Company (U.K.) Limited is a wholly-owned subsidiary of Nippon Fire and Marine Insurance Company, Limited (Japan).

Subsidiaries (except for wholly-owned): None.

North Atlantic Insurance Company, Limited

Parent Companies:
The parent company of North Atlantic Insurance Company, Limited (formerly known as British National Insurance Company Ltd.) is CI

Holdings Limited. The ultimate parent is Wingfield Limited.

Subsidiaries (except for wholly-owned): None.

Northern Assurance Company, Limited

Parent Companies:
The immediate parent of Northern Assurance Company, Limited is Commercial Union Assurance Company plc., which in turn, is a wholly-owned subsidiary of Commercial Union plc.

Subsidiaries (except for wholly-owned): None.

Norwich Union Fire Insurance Society Ltd.

Parent Companies:
Norwich Union Fire Insurance Society Ltd. is wholly-owned by Norwich Union Holdings plc. The ultimate holding company is Norwich Union Life Insurance Society.

Subsidiaries (except for wholly-owned): None.

Ocean Marine Insurance Company, Limited

Parent Companies:
Ocean Marine Insurance Company, Limited is a wholly-owned subsidiary of Commercial Union Assurance Company plc. The ultimate parent company is Commercial Union plc.

Subsidiaries (except for wholly-owned): None.

Orion Insurance Company, Limited

Parent Companies:
Orion Insurance Company, Limited is now known as Orion Insurance Company plc. It is a wholly-owned subsidiary of Nationale-Nederlanden NV which is, in turn, a wholly-owned subsidiary of Internationale Nederlanden Verzekeringen NV.

Subsidiaries (except for wholly-owned):
Orion Marine Insurance Underwriting Agency Limited.

Pearl Assurance Company, Limited

Parent Companies:
Pearl Assurance Company, Limited, now known as Pearl Assurance Public Liability Company, is a wholly-owned subsidiary of Pearl Group plc. The ultimate parent company is Australian Mutual Provident Society of Sidney, Australia.

Subsidiaries (except for wholly-owned): None.

Phoenix Assurance Company, Limited

Parent Companies:
The parent company of Phoenix Assurance Company, Limited is Phoenix Assurance plc.,

which in turn is wholly-owned by Sun Alliance and London Insurance plc.

Subsidiaries (except for wholly-owned): None.

Polaris Insurance Company, Limited

Parent Companies:
Polaris Insurance Company, Limited was merged into Uni Storebrand Insurance Company (UK) Limited, which is wholly-owned by Uni Storebrand International. The ultimate parent is Uni Storebrand A.S.

Subsidiaries (except for wholly-owned): None.

La Preservatrice Company Anoynyne D'Assurances

Parent Companies:
La Preservatrice Company Anoynyne D'Assurances is a subsidiary of Preservatrice Fonciere Tiard. Preservatrice Fonciere Tiard is controlled by Groupe Athena, the insurance holding company of Worms & Cie.

Subsidiaries (except for wholly-owned): None.

Provincial Insurance Company, Limited

Parent Companies:
Provincial Insurance Company, Limited is a subsidiary of Provincial Insurance plc., which in turn is owned by Provincial Group plc.

Subsidiaries (except for wholly-owned):
Provincial Insurance Company of East Africa, Ltd., Provincial Citystate Group Ltd.

Prudential Assurance Company, Limited

Parent Companies:
Prudential Assurance Company, Limited (also known as Prudential Insurance Company, Ltd.) is a subsidiary of Prudential Corporation, plc.

Subsidiaries (except for wholly-owned):
Prudential Life of Ireland, Limited; Prudential Vita SpA; St. Helen's Trust Limited and the Standard Trust Limited.

Prudential Trust Company, Limited

Parent Companies:
The parent company of Prudential Trust Company, Limited is Prudential Corporation, plc.

Subsidiaries (except for wholly-owned): None.

Riunione Adriatica Di Sicurta (RAS), Italy

Parent Companies:
The parent company of Riunione Adriatica Di Sicurta (RAS), Italy is Riunione Adriatica Di Sicurta, SpA. The parent company is 51.5% owned by ACIF Allianz Compagnia Italiana Finanziamenti SpA of Milan. Shares of Riunione

Adriatica Di Sicurta, SpA are traded on the Italian Stock Exchanges.

Subsidiaries (except for wholly-owned): None.

River Thames Insurance Company, Limited

Parent Companies:

The immediate holding company of River Thames Insurance Company, Limited is Transamerica Insurance Company which owns 51% of the company. The ultimate holding company is Transamerica Corporation. The remaining 49% is owned by Sedgwick Group plc.

Subsidiaries (except for wholly-owned): None.

Road Transport & General Insurance Company, Limited

Parent Companies:

Road Transport & General Insurance Company, Limited is a wholly-owned subsidiary of General Accident Fire & Life Assurance Corporation plc, which in turn, is a subsidiary of General Accident plc.

Subsidiaries (except for wholly-owned): None.

Royale Belge per Thilly Re, Belgium

Parent Companies:
The parent company of Royale Belge is Royal Belge S.A.

Subsidiaries (except for wholly-owned): None.

Royal Insurance Company (UK) Limited

Parent Companies:
Royal Insurance Holdings plc is the holding company and ultimate parent of the Royal Insurance Group, of which Royal Insurance Company (UK) Limited is a wholly-owned subsidiary company.

Subsidiaries (except for wholly-owned): None.

Royal Scottish Insurance Company, Limited

Parent Companies:
Royal Scottish Insurance Company, Limited, now known as the Royal Scottish Assurance Company, is wholly-owned by the Royal Bank of Scotland Group plc.

Subsidiaries (except for wholly-owned):
Royal Scottish Assurance Services Limited.

Scan Re Insurance Company, Limited

Parent Companies:
The parent companies of Scan Re Insurance Company Limited are by Gjensidige Forsikring (Norway) and Lansforsakringsbolagens A.B. (Sweden).

Scottish Lion Insurance Company, Limited

Parent Companies:
Scottish Lion Insurance Company, Limited is a wholly-owned subsidiary of China Merchants' Holding Co., Ltd.

Subsidiaries (except for wholly-owned): None.

Sirius Insurance Company, Limited

Parent Companies:
Sirius Insurance Company, Limited is a wholly-owned subsidiary of the Sirius Insurance Company Limited of Sweden. The ultimate parent is ABB Asea Brown Boveri.

Subsidiaries (except for wholly-owned): None.

Skandia Insurance Company (Sweden), Limited

Parent Companies:
Skandia Insurance Company (Sweden), Limited is part of Skandia Group, the ultimate parent is Skandia Insurance Company A.B.

Subsidiaries (except for wholly-owned): None.

Skandia (United Kingdom) Insurance Company, plc

Parent Companies:
Skandia (United Kingdom) Insurance Company, plc is a wholly-owned subsidiary of Skandia International Insurance Corporation, which in turn is a wholly-owned subsidiary of Skandia International Holding A.B.

Subsidiaries (except for wholly-owned): None.

Sovereign Marine & General Insurance Company, Limited

Parent Companies:
Sovereign Marine & General Insurance Company, Limited is a wholly-owned subsidiary of Willis Corroon Group plc.

Subsidiaries (except for wholly-owned): None.

Sphere Drake Insurance Company, Limited

Parent Companies:
Sphere Insurance Company Limited is now known as Sphere Drake Insurance plc. Its immediate holding company is Sphere Drake Insurance Group plc which is, in turn, wholly-owned by Sphere Drake Acquisitions Limited which is, in turn, wholly-owned by Sphere Drake Holding plc (U.K.), which is, in turn,

wholly-owned by Sphere Drake Limited which is, in turn, wholly-owned by Sphere Drake Holdings Limited (Bermuda).

Subsidiaries (except for wholly-owned): None.

Sphere Insurance Company, Limited

Parent Companies:

Sphere Insurance Company Limited is now known as Sphere Drake Insurance plc. Its immediate holding company is Sphere Drake Insurance Group plc which is, in turn, wholly-owned by Sphere Drake Acquisitions Limited which is, in turn, wholly-owned by Sphere Drake Holding plc (U.K.), which is, in turn, wholly-owned by Sphere Drake Limited which is, in turn, wholly-owned by Sphere Drake Holdings Limited (Bermuda).

Subsidiaries (except for wholly-owned): None.

Storebrand Insurance Company (United Kingdom), Limited

Parent Companies

Storebrand Insurance Company (United Kingdom), Limited, now known as Uni Storebrand Insurance Company (UK) Ltd., is wholly-owned by Uni Storebrand International, Limited. The ultimate parent is Uni Storebrand A.S.

Subsidiaries (except for wholly-owned): None.

Stronghold Insurance Company, Limited

Parent Companies:

Stronghold Insurance Company, Limited is a wholly-owned subsidiary of NW Reinsurance Corporation Limited. The ultimate holding company is Norwich Winterthur Holdings Limited. The holding company, in turn, is controlled by Norwich Union Insurance Group of the United Kingdom and Winterthur Swiss Insurance Company of Switzerland, each of which holds 48.5% of the shares of the parent company; the balance is held by the Chiyoda Fire and Marine Insurance Company (Europe) Limited.

Subsidiaries (except for wholly-owned): None.

The Svenska Veritas Marine and Fire Insurance Company, Limited

Parent Companies:

The Svenska Veritas Marine and Fire Insurance Company, Limited is a wholly-owned subsidiary of WASA International Insurance Company Limited, which is a wholly-owned subsidiary of WASA Insurance Holding Company, Limited.

Subsidiaries (except for wholly-owned): None.

Switzerland General Insurance Company (U.K.), Limited

Parent Companies:

Switzerland General Insurance Company (U.K.) Limited is a wholly-owned subsidiary of Switzerland General Insurance Company, which in turn, is owned by the Swiss Reinsurance Company, Zurich.

Subsidiaries (except for wholly-owned): None.

Terra Nova Insurance Company, Limited

Parent Companies:

Terra Nova Insurance Company, Limited is wholly-owned by Terra Nova Insurance Group plc.

Subsidiaries (except for wholly-owned): None.

Threadneedle Insurance Company, Limited

Parent Companies:

The immediate parent of Threadneedle Insurance Company, Limited is Eagle Star Insurance Company, Ltd, which is wholly-owned by Eagle Star Holdings plc., which is a wholly-owned subsidiary of BAT Industries plc.

Subsidiaries (except for wholly-owned): None.

Tokio Marine & Fire Insurance Company (U.K.), Limited

Parent Companies:
Tokio Marine & Fire Insurance Company (U.K.), Limited is a wholly-owned subsidiary of the Tokio Marine & Fire Insurance Company, Limited, Japan.

Subsidiaries (except for wholly-owned):
Tokio Marine Europe Ltd.
TM Management Services Ltd.

Trent Insurance Company, Limited

Parent Companies:
Trent Insurance Company Limited was merged into Eagle Star Insurance Company Limited, which is wholly-owned by Eagle Star Holdings plc. The ultimate holding company is BAT Industries plc.

Subsidiaries (except for wholly-owned): None.

Turegum Insurance Company, Limited

Parent Companies:
Turegum Insurance Company, Limited is a wholly-owned subsidiary of Zurich Insurance Company (also known as Zurich Versicherungs-Gesellschaft).

Subsidiaries (except for wholly-owned): None.

Ulster Marine Insurance Company, Limited

Parent Companies:
Ulster Marine Insurance Company Limited is a wholly-owned subsidiary of General Accident Fire and Life Assurance Corporation plc.

Subsidiaries (except for wholly-owned): None.

L'Unione des Assurance de Paris, France

Parent Companies:
The parent company of L'Unione des Assurance de Paris, France is Societe Centrale Union des Assurances de Paris.

Subsidiaries (except for wholly-owned): None.

USICO

Parent Companies:
USICO was a utility owned and operated industry mutual insurance company. As of March 1, 1990 USICO went into runoff. At that time, the owners of this mutual company were: Boston Edison; Carolina Power & Light; COM Energy; Freeport Power; Minnesota Power; Northeast Utilities; Pennsylvania Power & Light; San Diego G&E; Square Butte Electric Corp.; Superior Water, Light & Power; Texas Eastern Transmission Corp.; Texas Gas Transmission and Texas Utilities.

Vanguard Insurance Company, Limited

Parent Companies:

Vanguard Insurance Company, Limited, is 70% owned by the Broken Hill Proprietary Company Ltd. and 30% owned by Assicurazioni Generali SpA.

Subsidiaries (except for wholly-owned): None.

Vesta Insurance Company, Limited

Parent Companies:

The parent company of Vesta Insurance Company, Limited is Skadeforsikringsselskapet Vesta A/S (Norway). The ultimate holding company is Skandia Group Insurance Company Ltd.

Subsidiaries (except for wholly-owned): None.

Wausau Insurance Company (United Kingdom), Limited

Parent Companies:

Wausau Insurance Company (United Kingdom), Limited is a wholly-owned subsidiary of Employers Insurance of Wausau – A Mutual Company.

Subsidiaries (except for wholly-owned): None.

Westminster Aviation Insurance Group

Parent Companies:

None. Westminster Aviation Insurance Group is an underwriting agency whose main shareholders are GAN International, France; GAN Minster; Assurances Generales de France and CAMAT.

Subsidiaries (except for wholly-owned): None.

World Auxiliary Insurance Corporation, Limited

Parent Companies:

World Auxiliary Insurance Corporation, Limited is a wholly-owned subsidiary of Commercial Union Assurance Company plc which is, in turn, a wholly-owned subsidiary of Commercial Union plc.

Subsidiaries (except for wholly-owned): None.

World Marine and General Insurance Company, Limited

Parent Companies:

World Marine & General Insurance Company Limited is wholly-owned by the Broken Hill Proprietary Company Ltd.

Subsidiaries (except for wholly-owned): None.

Wurttembergische Feuer, United Kingdom

Parent Companies:

The main shareholders are the Swiss Re Group; Robert Bosch Gmbh; Baden – Wurttembergisch Bank AG and Commerzbank AG.

Subsidiaries (except for wholly-owned):

Nord-Deutsche Versicherungs–AG, Hamburg; Wurttembergische und Badische Verscicherungs–AG, Helbronn; Folgate Insurance Co. Ltd., London; Levensverzekering Maatschappij Erasmus N.V., Rotterdam; Allgemeine Rentenarstalt, Lebens und Rentenversicherungs–AG, Stuttgart; Baden-Wurttembergische Bank AG, Stuttgart; Baden-Wurttembergische Kapitalanlagegesellschaft mbH, Stuttgart and Unternehmensbeteiligungs-gesellschaft Baden-Wurttemberg AG.

Yasuda Fire & Marine Insurance Company (U.K.), Limited

Parent Companies:

Yasuda Fire & Marine Insurance Company (U.K.), Limited, now known as Yasuda Fire & Marine Insurance Co. of Europe, Ltd., is wholly-owned by Yasuda Fire & Marine Insurance Company Limited, Japan.

Subsidiaries (except for wholly-owned): None.

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Supreme Court, U.S.
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No. 93-2070

IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

TEXAS EASTERN TRANSMISSION CORPORATION,
Petitioner,

v.

FIDELITY & CASUALTY INSURANCE COMPANY OF NEW YORK, *et al.*,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

REPLY BRIEF FOR THE PETITIONER

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1. Respondents do not seriously dispute that the lower courts' determination that ICI is a "foreign state" under the FSIA conflicts with at least three nonappealable district court decisions in other Circuits. (Opp. 16-19 & n.8.) They argue, however, that this conflict is not worthy of this Court's review because (a) the conflict is primarily factual rather than legal in nature, and (b) a conflict involving unappealable district court decisions does not warrant a grant of certiorari. Neither point withstands scrutiny.

In order for ICI to qualify as a "foreign state" under the FSIA, "a majority of [its] shares or other ownership interest [must be] owned by a foreign state or political subdivision thereof." 28 U.S.C. § 1603(b)(2). The court in *Mobil Corp.* v. *Abeille Gen. Ins. Co.*, No. H-89-3877, 1990 WL 504828 (S.D. Tex. Nov. 6, 1990) (App. 332-39), *appeal dismissed*, 984 F.2d 664 (5th Cir. 1993), concluded that ICI did not fall within this statutory definition. *Mobil* construed Section 1603(b)(2) to require that the "legal title" of the shares or other ownership interests rest with the foreign government, which is not the case with ICI. (App. 334.) In addition, when, as with ICI, "other ownership interests" are relied on as the basis for the assertion of "foreign state" status, the *Mobil* court read the statute to require the consideration of two factors: "'the degree to which the entity discharges a governmental function, and the extent of state control over the entities operations.'" (*Id.*) (quoting *Edlow Int'l Co.* v. *Nuklearna Elektrarna Krsko*, 441 F. Supp. 827, 832 (D.D.C. 1977)). Two other district courts, in the Eighth and Ninth Circuits, have followed *Mobil*.[1/]

[1/] *Aluminum Co. of Am.* v. *Admiral Ins. Co.*, No. C93-32C (W.D. Wash. Apr. 9, 1993) (App. 313-15); *Murphy Oil USA, Inc.* v. *United States Fidelity & Guar. Co.*, No. 91-1157, 1992 WL 465701 (W.D. Ark. Dec. 21, 1992) (App. 316-31). Although the Eighth Circuit in *Murphy Oil* later ordered the district court to conduct a limited evidentiary hearing, *Murphy Oil USA, Inc.* v. *United States Fidelity & Guar. Co.*, No. 93-1207

(continued...)

The courts below, presented with the same factual representations as were made in *Mobil*, reached a different legal conclusion based upon a dramatically different understanding of Section 1603(b)(2). Unlike *Mobil*, the courts below did not require legal title to rest with the Government of Ireland. Nor did they interpret the FSIA to require consideration of the two additional factors recited in *Mobil* for determining foreign sovereign claims. Instead, they held that the "administration procedure," whereby the stock of ICI's holding company, SAT, was placed in trust for the benefit of the Irish Minister of Industry and Commerce, was sufficient to convert ICI into a "foreign state." (App. 23, 81, 295-98.)

Respondents attempt to denigrate the significance of these conflicting interpretations of the FSIA by claiming that ICI's status under the FSIA is a factual rather than a legal issue. There has never been any material dispute, however, in this case or in *Mobil*, *Murphy Oil*, or *ALCOA*, concerning the facts of ICI's relationship to the Irish government. The essential issue in all of these cases has been the legal significance under the FSIA of these undisputed facts. *Mobil*, *Murphy Oil*, and *ALCOA* applied one interpretation of the FSIA to these undisputed facts to reach one legal conclusion; the courts below applied another construction of the FSIA to these same

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1/(...continued)
(8th Cir. June 21, 1993) (Opp. RA1-RA3), the court of appeals never questioned the district court's legal analysis, which included a lengthy review of *Mobil* and an adoption of *Mobil*'s "persuasive" reasoning. (App. 330.) Moreover, soon after the court of appeals' limited remand order, ICI itself voluntarily dismissed the appeal, leaving the district court's opinion fully intact and fully in conflict with the decisions below. *Murphy Oil USA, Inc.* v. *United States Fidelity & Guar. Co.*, No. 93-1207 (8th Cir. Aug. 30, 1993) (Opp. RA4-RA5).

undisputed facts to reach the opposite legal conclusion.[2/] Indeed, respondents themselves tacitly admit that the conflict here is legal in nature. Although at times they assert that the issue is "fact-bound," they switch gears when discussing *Mobil*, attacking the merits of the decision as based on an improper construction of Section 1603(b)(2) — clearly a legal question. (Opp. 16-19.)[3/]

As explained in the Petition, the conflict here is the equivalent of a conflict in the Circuits. (Petn. 13.) Respondents do not dispute that a decision holding that a removing party is not a "foreign state" under the FSIA is not appealable. *See* 28 U.S.C. § 1447(d). Indeed, the Fifth Circuit in *Mobil*, in a published decision, expressly held that the district court's decision on the issue was final and unappealable. *Mobil Corp.* v. *Abeille Gen. Ins. Co.*, 984 F.2d 664 (5th Cir. 1993). At present, then, district courts in the Fifth Circuit apply one standard of FSIA removal and remand and district courts in the Third Circuit apply another. Because the Fifth Circuit is statutorily barred from reviewing the issue in this procedural context, only this Court can

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[2/] The Third Circuit's recitation of a "clearly erroneous" standard of review was directed solely to the undisputed, underlying facts, not to the legal conclusion based on these facts. (App. 22-23 & n.8.) It is well settled that the ultimate conclusion whether an entity constitutes a "foreign state" under the FSIA is a legal question of subject matter jurisdiction reviewable *de novo*. *See, e.g.*, *General Elec. Capital Corp.* v. *Grossman*, 991 F.2d 1376, 1380 (8th Cir. 1993).

[3/] Even if the lower courts' disagreement over the issue of ICI's status concerned a purely factual issue, review by this Court would nevertheless be appropriate. *See* R. Stern, *et al.*, *Supreme Court Practice* 189-90 (7th ed. 1993) ("Of course, if two courts of appeals have . . . made different findings of fact as to the same subject matter, certiorari may be granted to review either decision so as to preserve uniformity of decision among circuits.").

resolve the controversy.[4/] This Court has previously granted certiorari to review conflicts created by district courts in procedural contexts that are much less compelling than in this case.[5/]

Respondents attempt to minimize the importance of this conflict by contending that it "does not present an issue of importance to anyone other than the parties." (Opp. 12.) The existence of four entirely separate insurance coverage disputes in different Circuits — all involving ICI — belies this contention. Of course, the issue is not limited to disputes involving ICI; the "foreign state" issue in this case can and does arise in cases involving other insurers.

The most recent example of this phenomenon is the billion-dollar insurance coverage litigation arising from the *Exxon Valdez* oil spill. Exxon Corporation has sued its numerous insurers for coverage for the *Valdez* oil spill in Texas state court. On June 28, 1994, the successor to Norske Triton Insurance Company Limited, a Norwegian insurer,

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[4/] As respondents point out (Opp. 15), ICI's foreign sovereign status could be adjudicated outside of the removal context. It is no accident, however, that all three of the conflicting ICI decisions, as well as the *Texas Eastern* case below, arose in the removal context. Complex, multi-party insurance coverage disputes often involve nondiverse parties and are typically brought by policyholders who seek to have their state-law coverage claims decided in state courts. The *Exxon Valdez* insurance coverage litigation, discussed *infra* at 4-5, is another recent example of this phenomenon.

[5/] *See, e.g.*, *Gulf Offshore Co.* v. *Mobil Oil Corp.*, 453 U.S. 473, 477 n.3 (1981); *Newport* v. *Fact Concerts, Inc.*, 453 U.S. 247, 257 n.14 (1981); *Dawson Chem. Co.* v. *Rohm & Haas Co.*, 448 U.S. 176, 185 (1980); *Massachusetts* v. *United States*, 435 U.S. 444, 453 (1978); *Curtis* v. *Loether*, 415 U.S. 189, 191 n.2 (1974).

removed the entire case to federal court, arguing that it was a foreign state within the meaning of the FSIA.[6/] In support of this argument, Norske's successor has argued, like ICI here, that it has been placed under "public administration" and that its shares are indirectly held for the benefit of its government.[7/] In seeking a remand to state court, Exxon has relied on *Mobil*, *Murphy Oil*, and *ALCOA*, while acknowledging the conflicting Third Circuit precedent.[8/] The rapidly-growing insolvency of foreign insurers (see Petn. at 14-15) will only increase the significance of this conflict — especially now that the Third Circuit has, in a published opinion, affirmed the legitimacy of the "foreign state" removal maneuver in derogation of prior precedent on the issue.[9/]

[6/] *See* Notice of Removal, *Exxon Corp.* v. *Certain Underwriters at Lloyd's of London*, Nos. H-94-2216, -2217 (S.D. Tex. filed June 28, 1994).

[7/] *See* Brief in Support of Removal, *Exxon Corp.* v. *Certain Underwriters at Lloyd's of London*, Nos. H-94-2216, -2217 (S.D. Tex. filed June 28, 1994), at 6.

[8/] *See* Memorandum in Support of Motion to Remand, *Exxon Corp.* v. *Certain Underwriters at Lloyd's of London*, Nos. H-94-2216, -2217 (S.D. Tex. filed July 21, 1994), at 21.

[9/] Respondents make much of the fact that *Mobil*, *Murphy Oil*, and *ALCOA*, are not published in the Federal Supplement. (Opp. 15.) This fact is unsurprising, however, since these are procedural decisions remanding the cases to state court. The decisions are reported and analyzed in trade journals such as *Mealey's Insurance Litigation Reports* and are well-known in the insurance community. Moreover, as this case and the recent *Exxon Valdez* litigation demonstrate, courts and litigants continue to cite and rely on these decisions. *See also Tennessee Gas Pipeline Co.* v. *Continental Casualty Co.*, 814 F. Supp. 1302, 1306 n.6 (M.D. La. 1993) (noting that *Mobil*, *Murphy Oil*, and the district court decision below constitute "conflicting opinions" on this issue).

2. As explained in the Petition (Petn. 17-21), the lower courts' assumption of subject-matter jurisdiction over the claims against the nondiverse insurers in the *F&C* case conflicts with *Finley* v. *United States*, 490 U.S. 545 (1989), and *Birmingham Fire Ins. Co.* v. *Winegardner and Hammons, Inc.*, 714 F.2d 548 (5th Cir. 1983). Respondents attempt to distinguish the *F&C* case from *Finley* and *Birmingham Fire* by maintaining: (1) the *F&C* case involves "ancillary" rather than "pendent-party" jurisdiction; (2) the counterclaims against the nondiverse excess insurers were asserted by a defendant rather than a plaintiff; and (3) the new supplemental jurisdiction statute, 28 U.S.C. § 1367, renders the conflict with *Finley* and *Birmingham Fire* insignificant. These arguments are meritless.

Respondents' terminological quibbles about ancillary and pendent-party jurisdiction are beside the point.[10/] *Finley* defined pendent-party jurisdiction broadly as "jurisdiction over parties not named in any claim that is independently cognizable by the federal court." 490 U.S. at 549. That is exactly the situation here: The nondiverse excess insurers were not named in any claim over which the federal court had an independent basis of jurisdiction. *Finley* clearly prohibits the counterclaims against these parties, which are "added claims [which] involve added parties over whom no independent basis of jurisdiction exists." *Id.* at 551. Moreover, although *Finley* itself involved a construction of the Federal Tort Claims Act, the decision made clear that its analysis derived from, and applied to, pendent-party jurisdiction asserted in the diversity context. 490 U.S. at 552.

[10/] *See Aldinger* v. *Howard*, 427 U.S. 1, 13 (1976) ("there is little profit in attempting to decide . . . whether there are any 'principled' differences between pendent and ancillary jurisdiction").

Respondents also attempt to distinguish *Finley* from this case on the ground that *Finley* involved pendent-party claims asserted *by a plaintiff* while this case involved pendent-party claims asserted *by a defendant* "haled into court against its will." (Opp. 22-24.) This argument selectively relies on pre-*Finley* decisions and completely ignores the analysis of this very point in the two decisions that matter most for purposes of this Court's review — *Finley* and *Birmingham Fire*. *Finley* expressly rejected respondents' argument, and extended its prohibition on pendent-party jurisdiction to claims asserted by defendants and other parties "haled into court" involuntarily. 490 U.S. at 552-53 & n.6. (See Petn. 18-19.) Likewise, *Birmingham Fire* specifically rejected the plaintiff-defendant distinction as "not significant," and refused to permit a defendant to assert a counterclaim against a nondiverse party over which no independent basis of federal jurisdiction existed. 714 F.2d at 553. (See Petn. 19-20.) Respondents' citations of decisions that appear to embrace the plaintiff-defendant distinction highlight rather than diminish the conflict with *Finley* and *Birmingham Fire*,[11/] and confirm the need for review by this Court to resolve the controversy.

[11/] Respondents misleadingly assert that *Birmingham Fire* involved a noncompulsory counterclaim while the decision below involved a compulsory counterclaim. (Opp. 25-26.) In fact, in *both* cases the claim against the nondiverse parties was "most definitely not a compulsory counterclaim," 714 F.2d at 551, but rather was a new claim against new parties. *Birmingham Fire* is on all fours with the *F&C* case. In both cases, a plaintiff-insurer brought a state law coverage suit under the diversity statute, and the defendant-insured asserted counterclaims against the original plaintiff and attempted to join additional non-diverse insurers to the counterclaim for coverage arising from the same underlying accident. Although both courts relied primarily on this Court's decision in *Owen Equip. & Erection Co.* v. *Kroger*, 437 U.S. 365 (1978), they reached antithetical results concerning jurisdiction over the nondiverse counterclaim defendants. (See Petn. at 19-20.)

Respondents finally contend that the supplemental jurisdiction statute, 28 U.S.C. § 1367, deprives the conflict concerning pendent-party jurisdiction of lasting significance. This contention reveals a fundamental misunderstanding about the nature of the statute and the continuing significance of *Finley* to cases, like the *F&C* case, that are premised on diversity jurisdiction.

In subsection (a) of Section 1367, Congress overruled *Finley*'s holding concerning pendent-party jurisdiction with respect to cases involving federal question jurisdiction. Subsection (b) of Section 1367, however, codified the rule of complete diversity announced in *Owen Equip. & Erection Co.* v. *Kroger*, 437 U.S. 365 (1978). *See* H.R. Rep. No. 734, 101st Cong., 2nd Sess., 1990, at 29 n.16, *reprinted in* 1990 U.S. Code Cong. & Adm. News 6860, 6875 n.16. *Finley*'s identical rule of complete diversity also derived from *Kroger*. *See* 490 U.S. at 552-53.[12/] The applicability of that rule to counterclaims asserted against nondiverse parties is precisely the issue that has divided the Fifth and Third Circuits. Section 1367 therefore does not reduce the significance of the jurisdictional question raised by the petition: A decision regarding the existence of pendent-party jurisdiction over counterclaims brought against nondiverse parties will apply equally to cases brought before and after the enactment of Section 1367.

[12/] Like the complete diversity rule of *Kroger* and *Finley*, the reference in Section 1367(b) to claims by "plaintiffs" includes counterclaims by defendants against nondiverse parties. *See, e.g., 6247 Atlas Corp.* v. *Marine Ins. Co., Ltd.*, No. 92 Civ. 7064 (RWS), 1994 U.S. Dist. LEXIS 5514, at *12 (S.D.N.Y. April 26, 1994); *Mayatextil, S.A.* v. *Liztex U.S.A., Inc.*, No. 92 Civ. 4528 (LJF), 1993 U.S. Dist. LEXIS 6527, at *7 (S.D.N.Y. May 18, 1993); *see also* C. Wright, *The Law of the Federal Courts* 574 & n.71 (5th ed. 1994).

3. Respondents insinuate that a judgment in favor of petitioner would not change the result in this case because some portion of the *F&C* case might still remain after remand and might operate as "collateral estoppel." (Opp. 8-9, 20-21.) It is telling that respondents cite no authority for this proposition. In fact, the Third Circuit squarely rejected this argument: In their opposition to TETCO's petition for rehearing, respondents argued that TETCO's jurisdictional challenges were "moot" in light of the judgment in the *F&C* case. *See* Appellees' Joint Response to Petition for Rehearing (filed July 12, 1993), at 11-14. The appeals court nevertheless granted rehearing and proceeded to address the jurisdictional bases in all three of the consolidated cases. As Judge Alito noted in his dissent, the determinations of the portion of the *F&C* judgment that should be preserved (if any) in light of the jurisdictional errors and the effect of such a judgment on claims against other insurers involve complex factual and procedural questions that must be decided in the first instance on remand. (App. 47-48.)

CONCLUSION

For the foregoing reasons, and those stated in the Petition, it is respectfully submitted that a petition for a writ of certiorari should be granted.

Respectfully submitted,

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